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THE REVISED MODEL BUSINESS CORPORATION ACT AND CORPORATE LAW REFORM IN MISSISSIPPI: PART TWO

*Wendell H. Holmes**

In the 1987 Regular Session of the Mississippi Legislature, a new business corporation act for Mississippi (hereinafter New MBCA) became a reality.[1] The new law became effective January 1, 1988.[2] It is based almost entirely upon the Revised Model Business Corporation Act (hereinafter RMA) and profoundly changes much of the state's pre-existing corporate law. Part One of this article,[3] completed prior to the passage of the New MBCA, discussed in detail the relationship of the provisions of the RMA to the prior Mississippi Business Corporation Act (hereinafter Old MBCA) and proposed changes in Mississippi law (including substantial revisions to much of the RMA)[4] in the areas of corporate formation and organization, and corporate management and governance. That work now serves as the author's critique of the New MBCA regarding those topics.[5] The methodology of Part Two of this article will, logically, be somewhat different from that of Part One. Whereas the earlier installment was primarily an analysis of existing Mississippi law with proposals for revision (using the RMA as the point of departure for the revision process), this Part will undertake a critical analysis of the New MBCA in those areas not covered in Part One: capitalization, shareholder litigation, organic changes, and the problems of the closely-held business.

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[1] Mississippi Business Corporation Act, 1987 Miss. Laws Ch. 486 [hereinafter New MBCA], *codified at* Miss. Code Ann. §§ 79-4-1.01 to-17.04 (Supp. 1987). The New MBCA repeals the former statute, Miss. Code Ann. §§ 79-3-1 to-293 (1972 and Supp. 1986) [hereinafter Old MBCA] in its entirety.

[2] The New MBCA is to a large degree an outgrowth of the work of the Business Law Reform Task Force convened by Secretary of State Dick Molpus in July, 1986. The Task Force undertook to draft proposed legislation to replace the existing business corporation, nonprofit corporation, professional corporation, limited partnership, and securities acts. The author was a member of the Task Force and of the subcommittee responsible for drafting the proposed business corporation act. The views expressed in this article are solely those of the author and do not represent in any way those of any other person affiliated with the Task Force.

Among the other legislation that was generated by the Task Force is a new nonprofit corporation act which closely parallels the New MBCA. This act is labeled the Mississippi Nonprofit Corporation Act, 1987 Miss. Laws Ch. 485, *codified at* Miss. Code Ann. §§ 79-11-101 to-399 (Supp. 1987).

[3] Holmes, *The Revised Model Business Corporation Act and Corporate Law Reform in Mississippi: Part One*, 56 Miss. L.J. 165 (1986) [hereinafter *Part One*].

I. CAPITALIZATION

A. *Par Value, Stated Capital, and Distributions*

By far the most revolutionary aspect of the New MBCA (at least in contrast to traditional Mississippi practice) is section 6.40.[6] In one swift motion, the concepts of par value, stated capital, earned surplus, capital surplus, and treasury stock were swept from the corporate statutes. The approach of the New MBCA to these areas is particularly striking in light of some highly idiosyncratic provisions of prior Mississippi law.

Specifically, under the Old MBCA, the minimum permissible par value of stock was $1.00.[7] Moreover, while no-par stock was ostensibly permitted, any practical advantage of the concept was undercut by the statute's insistence that the *issue* price of no-par stock not be less than $1.00.[8] Thus the *raison d'etre* of no-par stock, *i.e.*, the elimination of "watered stock" liability, was completely defeated.[9] These aspects of the Old MBCA deprived corporate planners, arguably without justification,[10] of a substantial degree of flexibility in matters involving a corporation's stock structure.[11]

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[4] It might be noted that *Part One* was completed prior to the finalization of the work of the Task Force.

[5] The New MBCA uses the same numerical system as the RMA, resulting in easy cross-reference. In addition, while the New MBCA (as is typical of Mississippi legislation) includes no published commentary and little legislative history, the Official Comments to the RMA should constitute persuasive authority regarding the interpretation of the new act.

[6] *See* New MBCA, *supra* note 1, § 6.40. The new act adopts without change the corresponding provision of the RMA. REVISED MODEL BUSINESS CORP. ACT § 6.40 (1984).

[7] Old MBCA, *supra* note 1, § 33.

[8] *Id.*

Criticism of the par value concept has long been widespread, and the breach in the dam occurred in 1975 when California eliminated the requirement of a statement of par value of authorized shares.[12] The ABA Committee on Corporate Laws took up the torch in 1979,[13] and its approach was reflected in the RMA and, correspondingly, by the New MBCA.

The mere elimination of par value, however, might not appear at first blush to be that significant of a change. It is only in its relation to the question of dividends and distributions that its true importance is manifested.

The Old MBCA was a traditional "earned surplus" statute.[14] Under its provisions, the par value of shares issued with a par value, or (absent any contrary allocation by the board of directors) the full consideration for no-par shares was committed to stated capital.[15] The excess, if any, became capital surplus. Under ordinary circumstances, capital surplus could not be distributed to shareholders. Rather *dividends* (cash or property) could be paid only out of the "unreserved and unrestricted earned surplus"[16] of a corporation, defined basically as the "balance of its net profits, income, gains and losses."[17] In contrast, *distributions* (cash or property) from capital surplus[18] were prohibited absent authorization in the articles of incorporation or by two-thirds of the shareholders, and were subject to other conditions involving the protection of senior security holders.[19]

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[9] For discussion of this issue under the Old MBCA, see Hodge & Perry, *The Model Business Corporation Act: Does The Mississippi Version Lime The Bushes*?, 46 MISS. L.J. 371, 380-81 (1975) [hereinafter Hodge & Perry] (liability of shareholder for watered stock).

[10] The historical rationale for the concept of par value has generally been twofold: to assure equitable contributions among shareholders by requiring that they pay a standard price ("par") for their shares; and to provide a "cushion" of capital to which creditors of the corporation would have recourse. *See* B. MANNING, A CONCISE TEXTBOOK ON LEGAL CAPITAL 19, 22 (2d ed. 1981) [hereinafter MANNING, LEGAL CAPITAL] (general background of development of legal capital concept). That neither premise applies today is clear. Under current practice par value establishes only the *minimum*, not the actual, issue price of shares. In addition, even under statutes such as the Old MBCA which prescribed a minimum capital contribution as a condition of doing business, the amount mandated (generally $1000) was insufficient to provide any meaningful protection to creditors. *See* Old MBCA, *supra* note 1, § 111; Hodge & Perry, *supra* note 9, at 379.

[11] *See* Hodge & Perry, *supra* note 9, at 381-82.

[12] 1975 Cal. Stat. 682, § 7, *codified at* CAL. CORP. CODE § 202(d)(e).

[13] Committee on Corporate Laws, *Changes in the Model Business Corporation Act - Amendments to Financial Provisions*, 34 BUS. LAW. 1867 (1979) [hereinafter *Financial Provisions*] (amendments and comments of committee). The proposed changes were finally approved for inclusion in the Model Act in 1980. Committee on Corporate Laws, *Changes in the Model Business Corporation Act-Amendments to Financial Provisions*, 35 BUS. LAW. 1365 (1980).

[14] For a general discussion of such statutes, see MANNING, LEGAL CAPITAL, *supra* note 10, at 72-75.

This much of the Old MBCA was representative of most earned surplus statutes; the exact parameters of a corporation's discretion in these matters was, however, clouded by an additional, non-uniform provision of the Old MBCA specifically prohibiting *cash* dividends unless paid out of unreserved and unrestricted earned surplus.[20] As previously discussed in some

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[15] *See* Old MBCA, *supra* note 1, § 39. If no-par shares were issued, at least $1.00 per share was required to be allocated to stated capital. *Id.*

[16] *Id.* § 83(a).

[17] *Id.* § 3(m). Stock dividends, however, could be issued out of any treasury shares reacquired out of surplus (presumably earned or capital), and out of authorized but unissued shares so long as appropriate amounts of "any unreserved and unrestricted surplus" were transferred to stated capital. *Id.* § 83(c), (d).

[18] *Id.* § 3(1), (n). "Surplus" was defined as "the excess of the net assets of a corporation over its stated capital." "Capital surplus" was "the entire surplus of a corporation other than its earned surplus." *Id.* Functionally, capital surplus generally represented the excess (if any) of the issue price of shares over their par value.

[19] *Id.* § 85. Neither dividends nor distributions from capital surplus could be made if the corporation was insolvent or would thereby be rendered insolvent.

The use of the label "distributions" was, of course, a distinction without a difference, since the economic effects on shareholders and the corporation were identical in either event; only the nature of the accounting transaction involved was in any way affected.

[20] *Id.* § 87. The full text of the statute was as follows:

> Anything to the contrary in this chapter notwithstanding, the board of directors of a corporation shall never declare, nor shall a corporation pay, a cash dividend unless such dividend is out of the unreserved and unrestricted earned surplus only of such corporation and has been legally appropriated for the specific purpose of paying dividends; provided further, that no such dividend shall be declared or paid when the corporation is insolvent or when the payment thereof would render the corporation insolvent or when such payment would

detail in Part One, the full import of this additional restriction, particularly on the ability of a corporation to make *cash* distributions from capital surplus, has never been clear.[21] Unless one were willing to rely upon the frankly artificial bifurcation of "dividends" and "distributions,"[22] the Old MBCA made any such cash distributions of dubious legality.[23]

The drafters of the RMA recognized the irrationality of the earned surplus test as a device for protecting creditors and senior security holders from payments to junior security holders. Thus, in addition to eliminating the concepts of stated capital and par value, they subjected distributions to shareholders to the sole restriction of insolvency,[24] at the same time consolidating under the classification "distributions" transactions previously denominated as dividends, distributions, share repurchases, redemptions, and distributions in liquidation.

Thus, under section 1.40 of the New MBCA, a "distribution" is defined as "a direct or indirect transfer of money or other property (except its own shares) or incurrence of indebtedness by a corporation to or for the benefit of its shareholders," and may take the form of "a declaration or payment of a divi-

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> be contrary to any provisions in the articles of incorporation. Nothing in this chapter shall impair or prevent a legal distribution to shareholders upon liquidation or dissolution as provided in this chapter.

Id.

[21] *See* Hodge & Perry, *supra* note 9, at 377-79.

[22] *See* note 19 *supra.*

[23] The statute could be circumvented, however, either by a redemption of stock out of capital surplus, or possibly by a property (in kind) distribution. *See* Hodge & Perry, *supra* note 9, at 378-79.

[24] *See* 1 MODEL BUSINESS CORP. ACT ANN. 484 (3d ed. 1985) (annotation notes that insolvency restriction was significant limitation on distributions); *Financial Provisions*, *supra* note 13, at 1867-68 (supporting adoption of more rigid stated capital requirements).

It should be noted that this response to the inadequacy of stated capital provisions is not an inevitable one; arguments have been advanced that the proper approach would be the adoption of a more realistic minimum amount of stated capital which could not be reduced. *See, e.g.*, Note, *The Inadequacy of Stated Capital Requirements*, 40 U. CIN. L. REV. 823, 841 (1971) (article uses trust fund theory approach to justify increased stated capital requirements). In effect this adopts the "trust fund" concept of Wood v. Dummer, 30 F. Cas. 435 (No. 17,944)(C.C.D. Me. 1824). The logistical difficulties in both formulating that "realistic" amount and in policing its maintenance make this a somewhat utopian proposal.

dend; a purchase, redemption or other acquisition of shares; a distribution of indebtedness; or otherwise."[25]

The heart of the financial provisions, however, is section 6.40. Under subsection (a), the board may authorize and the corporation may make distributions to shareholders subject only to the restrictions of the articles (if any) and of subsection (c). The statutory restriction adopts the twofold standard of equity and balance sheet solvency.[26] Thus, a distribution cannot be made if, after giving effect to it, the corporation cannot pay its debts as and when they became due (insolvency in the equity sense) or the corporation's total assets will be less than its total liabilities, together with the amount required to satisfy the liquidation rights of senior security holders (insolvency in the balance sheet sense).[27]

The obvious merit of the new scheme is the flexibility it provides to corporate managers. Ironically, this flexibility may engender the criticism that the new system gives inadequate guidance to directors, many of whom (particularly in the closely-held corporation which is the norm in Mississippi) may lack the requisite financial sophistication to make the judgments that the statute demands.

Such criticisms are addressed only in part by the statute. Section 6.40(d) allows directors to rely upon financial statements prepared on the basis of accounting practices which are reasonable under the circumstances, on a fair valuation, or any other method reasonable under the circumstances.[28] The matter of timing is governed by subsection (e), under which the effect of a distribution is determined in most cases as of the date of authorization, or the date of payment if more than 120 days after authorization.[29] In all other respects the statute is silent as to factors that should guide the board's determination of whether solvency (particularly in the equity sense) will be impaired; due to the absence of any substantial case authority, the Official Comments to the RMA provide the only persuasive guidance on this issue.[30] In any event, while under new section 8.33, adopted in 1988, consenting directors are expressly subjected to personal liability for illegal distributions, that liability is enforced only to the extent that the director's conduct violates the duty of care embodied in section 8.30 of the New MBCA and is not shielded by the business judgment rule.[31] Thus, most misjudgments will not be actionable.

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[25] New MBCA, *supra* note 1, § 1.40(6).

[26] *See Financial Provisions*, *supra* note 13, at 1868.

[27] *See* New MBCA, *supra* note 1, § 6.40(a),(c). Under the Old MBCA, "insolvency" meant only equity insolvency. *See, e.g.*, Old MBCA, *supra* note 1, § 3(o).

It should be noted that § 6.40 of the RMA has already been subject to an official amendment regarding the determination of insolvency. Under that amendment, codified as § 6.40(g), any indebtedness which by its terms can only be repaid to the extent that a distribution could be made is not treated as a liability under § 6.40(c). *See* Committee on Corporate Laws, *Changes in the Model Business Corporation Act - Amendments Pertaining to Distributions*, 42 BUS. LAW. 259 (1986), 42 BUS. LAW. 1207 (1987) (amendments and comments). This amendment was adopted in Mississippi in 1988. MISS. CODE ANN. § 79-4-6.40(g)(Supp. 1988).

[28] This terminology deliberately omits reference to technical accounting jargon and specific concepts such as "generally accepted accounting principles." REVISED MODEL BUSINESS CORP. ACT § 6.40 Official Comment 4 (1984).

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[29] *See* New MBCA, *supra*, 1, § 6.40(e)(3). Special rules are stated for distributions by purchase, redemption or other acquisition of shares, in which case the operative date is the earlier of the date money or property is transferred or debt is incurred, or the date the shareholder ceases to be a shareholder with respect to the acquired shares; and for other distributions of indebtedness, in which case the operative date is the date of distribution. *Id.* § 6.40(e)(1)-(2). This provision resolves the conflict posed in cases such as Williams v. Nevelow, 513 S.W. 2d 535 (Tex. 1974), in which the court held that for a corporation repurchasing shares in exchange for an installment promissory note, solvency was to be determined as of the time of the issuance of the debt instrument, not as of the time of each subsequent installment payment on the debt. The New MBCA embraces the rule of *Williams*.

[30] Revised Model Business Corp. Act § 6.40 Official Comment 2 (1984). The comments state that decisions involving equity insolvency should be "based on a cash flow analysis that is itself based on a business forecast and budget for a sufficient period of time to permit a conclusion that known obligations of a corporation can reasonably be expected to be satisfied over the period of time that they will mature." *Id.* Reliance solely upon a comparison of current assets to current liabilities, or of the present liquidation value of assets to existing liabilities, is eschewed. *Id.* In any event, the same decisions were required under the Old MBCA, which adopted the equity insolvency test. Old MBCA, *supra* note 1, § 3(o).

[31] Miss. Code Ann. § 79-4-8.33 (Supp. 1988). The same result would have obtained under the New MBCA as originally enacted. *See Financial Provisions*, *supra* note 13, at 1882. The new statute adds express rights of contribution against other culpable directors and shareholders who accepted the distribution knowing of the violation (which includes violations of the articles). *Id.* § 79-4-8.33(b). Any action must be commenced within two years of the date determined by § 6.40(c) or (g). *Id.* § 79-4-8.33(c).

Section 8.30 of the New MBCA is identical to its counterpart in the RMA; for an extensive discussion of those provisions and the related business judgment rule, see *Part One*, *supra* note 3, at 188-202. Of course, any decision tainted by self-dealing would be outside of the protection afforded by § 8.30.

B. Shares

Corresponding to the changes involving par value and related concepts, the New MBCA differs substantially from its predecessor in its treatment of authorized shares. The New MBCA contains no reference to the traditional classification of "common" and "preferred" shares. Rather, the statute mandates only that there be at least one class of stock with unlimited voting rights, and at least one class of stock which is entitled to receive the net assets of the corporation in dissolution.[32] If more than one class of stock is authorized then the articles must prescribe a distinguishing designation for shares (which, presumably, could include the terms common or preferred) but no legal significance is attached to the nomenclature used.[33] Rather, of paramount importance under the New MBCA is the *statement* of preferences, limitations and relative rights contained in the articles — in the words of the Official Comments to the RMA, the "contract" between the owners of these shares and the corporation with respect to their interests.[34] Except as permitted for series of shares all shares of a class must have identical rights.[35] As under the Old MBCA provisions on preferred stock, the variable rights and preferences permitted by the statute (which declares itself nonexclusive) include voting rights,[36] redemption or conversion features,[37] and dividend and liquidation preferences.[38] As was true under the Old MBCA,[39] the new statute provides for the issuance of classes of shares in series (so-called "blank stock") under which the board of directors, if so authorized by the articles of incorporation, can define the precise terms of each series by appropriate amendment to the articles at the time of issuance.[40]

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[32] New MBCA, *supra* note 1, § 6.01(b). Of course these rights may be consolidated in one class.

[33] *Id.* § 6.01(a). A possible exception to this is suggested by the RMA Comments, which state that if the fundamental rights of voting and residual equity interest are reposed in a single class of stock, that class may be described as simply "common shares." REVISED MODEL BUSINESS CORP. ACT § 6.01 Official Comment 1 (1984).

[34] REVISED MODEL BUSINESS CORP. ACT §6.01 Official Comment 1 (1984).

[35] *See* New MBCA, *supra* note 1, § 6.01(a).

[36] *Id.* § 6.01(c)(1). It should be noted that, as originally adopted, the New MBCA would not have permitted nonvoting common stock, pursuant to the mandate of MISS. CONST. art. 7, § 194. On November 10, 1987, the electorate approved Senate Concurrent Resolution No. 550 of the 1987 Regular Session of the Mississippi Legislature which repealed § 194. The original language of the New MBCA made nonvoting common stock permissible unless prohibited by § 194. New MBCA, *supra*, note 1, § 6.01(c)(1). The 1988 amendments to the New MBCA now simply sanction nonvoting shares generally. MISS. CODE ANN. § 79-4-6.01(c)(1) (Supp. 1988).

As under the former statute,[41] the New MBCA permits the issuance of fractional shares or scrip.[42] Holders of fractional shares have voting and proprietary rights; holders of scrip do not in the absence of contrary provision. The major innovation in the new law is that the board is now given the option of paying a shareholder the monetary value of fractional shares, or to "arrange for disposition of fractional shares," in addition to the issuance of fractional shares or scrip.[43]

As previously noted,[44] among the traditional corporate law notions abandoned by the New MBCA is that of treasury shares.[45] The drafters of the RMA concluded that the distinction between treasury shares and authorized but unissued shares was both unnecessary and, from many perspectives, undesirable.[46] Thus, under the New MBCA, shares acquired by the corporation are deemed to be authorized but unissued shares unless the articles prohibit their reissuance; in that event they are cancelled, and the statute permits the directors to file without shareholder action an amendment to the articles reflecting the decrease in the number of authorized shares.[47] Since the economic effect of the transaction is essentially that of a distribution of corporate assets, any reacquisition is within the definition of distribution and subject to the restrictions of section 6.40.[48]

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[37] *Id.* § 6.01(c)(2). The New MBCA changes existing law in this regard in one significant respect. Under the Old MBCA the right to redeem shares was limited to the option of the corporation. Old MBCA, *supra* note 1, § 27(a). Under the New MBCA redemption may be authorized at the option of the shareholder, another person, or upon the occurrence of a designated condition. New MBCA *supra* note 1, § 6.01(c)(2). Moreover, the price at which conversion or redemption is to occur may either be fixed by the articles, or may be determined by the use of a designated formula or by reference to extrinsic data or sources. *Id.* at § 6.01(c)(1-2).

[38] *See* New MBCA, *supra* note 1, § 6.01(c)(3), (4).

[39] *See* Old MBCA, *supra* note 1, § 29.

[40] *See* New MBCA, *supra* note 1, § 6.02. In this fashion, the board "fills in the blanks" in previously authorized shares. Such amendments require no shareholder action. *Id.* at § 6.02(d)(4).

[41] *See* Old MBCA, *supra* note 1, § 45.

[42] *See* New MBCA, *supra* note 1, § 6.04.

[43] *Id.* § 6.04(a)(1),(2). The "cash out" option is frequently employed in "going private" transactions. REVISED MODEL BUSINESS CORP. ACT § 6.04 Official Comment (1984).

[44] *See supra* text accompanying notes 6 and 7.

[45] *See* Old MBCA *supra* note 1, § 3(i). Those shares that were issued but reacquired by the corporation, and were held by the corporation rather than being cancelled or restored to the status of authorized but unissued shares were considered issued but not outstanding. *Id. See also* New MBCA, *supra* note 1, § 6.01(2).

Together with the elimination of par value, stated capital and surplus, the New MBCA substantially modifies the rules involving the consideration for issuance of shares and its allocation. The Old MBCA, like most traditional statutes, limited the permissible consideration for shares to money, tangible or intangible property, or services actually performed; promissory notes were specifically prohibited. The judgment of the board as to the value of consideration received was conclusive absent fraud.[49]

Substantially greater flexibility is provided under the new act, which adds promissory notes, contracts for future services, and other securities of the corporation to the roster of eligible forms of consideration.[50] The board is required to determine the value of consideration received or to be received but only for the purpose of determining that the shares are validly issued, fully paid and nonassessable; its determination is declared conclusive for these purposes.[51] The "fraud" standard placed on the discretion of the board is eliminated; liability for improper issuance of shares is thus governed by the ordinary duty of care of section 8.30 and the conflict of interest provisions of section 8.31.[52]

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[46] Revised Model Business Corp. Act § 6.31 Official Comment (1984).

[47] *See* New MBCA, *supra* note 1, § 6.31.

[48] *See* New MBCA, *supra* note 1, §§ 1.40(6), 6.40; Revised Model Business Corp. Act § 6.31 Official Comment (1984). *See also supra* notes 6, 28 and accompanying text. Under the Old MBCA shares could be repurchased only out of earned surplus, by article authorization or two-thirds approval of shareholders, or capital surplus. Old MBCA, *supra* note 1, § 9. Exceptions existed for purchases made to eliminate fractional shares, collecting or compromising debts, payments under dissenters' rights, and redemption or purchase to return redeemable shares. *Id.* § 9 (a-d). Under the New MBCA the twofold insolvency test would be the sole limitation on any reacquisition. *See, e.g.*, New MBCA, *supra* note 1, § 6.40(c).

[49] *See* Old MBCA, *supra* note 1, § 35.

[50] *See* New MBCA, *supra* note 1, § 6.21(b). An exception was made in the 1987 act for transportation corporations, due to a constitutional limitation applicable to such entities for money, property actually received, or labor done (or in good faith agreed to be done). Miss. Const. art. 7, § 195; New MBCA, *supra* note 1, § 6.21(F). Senate Concurrent Resolution No. 548 of the 1987 Regular Session of the Mississippi Legislature, repealing § 195, was approved by the electorate on November 10, 1987. An amendment was adopted in 1988 to the statute to remove the special rule stated in § 6.21. Miss. Code Ann. § 79-4-6.21 (Supp. 1988). The statute provides for protective mechanisms, such as

Due to the elimination of the par value and stated capital concepts, the board is no longer required to allocate consideration received for shares to "stated capital" and "surplus" accounts,[53] as was mandated by prior law.[54]

As under prior law,[55] a shareholder's liability is limited to the agreed consideration under section 6.20 or as provided in a subscription agreement;[56] the new statute also expressly insulates shareholders from personal liability for corporate obligations except those for which his own conduct creates liability.[57]

The New MBCA also makes an important change in prior law dealing with stock options. Under the Old MBCA any option issued as a means of compensation to directors, officers, employees or subsidiaries, not part of a general issuance to other share-

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deposit of shares in escrow, when shares are issued for notes or future services. *Id.* § 6.21(e).

[51] *Id.* § 6.21(c),(d).

[52] Revised Model Business Corp. Act § 6.21 Official Comment (1984).

[53] *Id.* Of course the statute does not prohibit the use of such categories as an accounting matter, if the board desires. *Id.*

[54] *See* Old MBCA, *supra* note 1, § 39.

[55] *Id.* § 47.

[56] New MBCA, *supra* note 1, § 6.20. These provisions do not substantially deviate from the prior statute. *See* Old MBCA, *supra* note 1, § 31.

[57] *See* New MBCA, *supra* note 1, § 6.22. The statute does permit, however, the imposition of such liability by a provision in the articles. *Id.* §§ 2.02(b)(2)(v), 6.22(b).

The New MBCA, then, eliminates any potential for "watered stock" liability based solely upon the issuance of shares below an artificially determined price. Rather, problems of overreaching, unfairness or unequal treatment are now placed under the broader penumbra of the board's fiduciary obligations. *See* Revised Model Business Corp. Act. § 6.21 Official Comment (1984); *Financial Provisions*, *supra* note 13, at 1879.

A special rule permits the issuance of shares to existing shareholders without consideration (*i.e.*, as a stock dividend or stock split) so long as this is done on a pro rata basis, and such issuance does not dilute the interests of a class of stockholders without their approval. *See, e.g.*, New MBCA, *supra* note 1, § 6.23(a)(b).

It should be noted that, in all events, the sole power to issue stock can be reserved to the shareholders in the articles. *Id.* § 6.21(a).

holders, required the approval of a majority of shareholders.[58] This provision was an indefensible restriction on the board's discretion, given the widespread acceptance of incentive compensation plans, and extrinsic rules requiring their disclosure in most public companies.[59] Thus the New MBCA deletes the requirement of shareholder approval altogether, rendering the matter one of business judgment and fiduciary duty of the board.[60]

C. *Preemptive Rights*

As under prior law,[61] the New MBCA makes preemptive rights[62] elective; that is, they do not exist unless so provided in the articles.[63] The Old MBCA did not, however, address the content of preemptive rights if only the mere election to provide them was made; with little Mississippi case law to consult for guidance one would have to divine the effect of the grant of "preemptive rights" from other common law authority.[64] Section 6.30 of New MBCA, which statutorily defines the presumptive effect of preemptive rights, is arguably an improvement over the silence of its predecessor. However, it erects traps for the unwary that should be carefully scrutinized by planners.

Specifically, under the New MBCA, a statement that the corporation elects preemptive rights, without any express provision to the contrary, will not entitle shareholders to exercise preemptive rights with respect to (a) shares issued as compensation to directors, officers, agents, employees, subsidiaries or affiliates, or to satisfy conversion or option rights created as compensation to any of those persons; (b) originally authorized shares issued within six months of incorporation; and (c) shares issued for consideration other than money (*e.g.*, property or services).[65] Moreover, preemptive rights are denied to shares with limited voting rights but preferential distribution rights; shares with general voting rights but no preferences have no rights to shares with preferences unless those shares are convertible into shares without preferences.[66] Finally, if shares subject to preemptive rights are not acquired by shareholders, they can be offered to third parties for a period of one year at a price not less than that at which they were offered to the shareholder; an offer at a lower price or after one year again invokes the preemptive right.[67]

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[58] *See* Old MBCA, *supra* note 1, § 37.

[59] *See* 17 C.F.R. § 240.14a-101 (1987)(disclosure of compensation plans in proxy statements of corporations registered under § 12(g) of Securities Exchange Act of 1934).

Moreover, as the comments to the RMA point out, approval may be required by stock exchange rules. REVISED MODEL BUSINESS CORP. ACT § 6.24 Official Comment (1984).

[60] *See* New MBCA, *supra* note 1, § 6.24.

[61] *See* Old MBCA, *supra* note 1, § 49.

[62] *I.e.*, the right of existing shareholders to acquire their proportionate share of any new issuance of stock before sales to others. H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS § 174 (2d ed. 1983) [hereinafter HENN & ALEXANDER]. *See* New MBCA, *supra* note 1, § 6.30.

[63] *See* New MBCA, *supra* note 1, § 6.30.

[64] The generally accepted view was that preemptive rights did not attach to treasury shares, shares issued for non-cash consideration, or shares issued in connection with a merger or consolidation; a split of authority existed as to whether they applied to originally authorized but unissued shares. *See* HENN & ALEXANDER, *supra* note 62, § 174, at 439-40.

Preemptive rights generally are not utilized in the public corporation arena but are frequently encountered as a protective device for minority shareholders in closely-held corporations.[68] This being the case, it must be noted that the New MBCA creates various avenues whereby a majority interest can effectively avoid the right—for example, by issuing shares as compensation to a majority director or officer or by issuing shares for property or services. While any such action taken as an oppressive measure could trigger liability for breach of fiduciary duty,[69] lengthy and expensive litigation may be necessary on the shareholder's part to assert the right to maintain his proportionate position. Thus, planners representing minority shareholders should consider the inclusion of appropriate provisions in the articles to broaden the scope of preemptive rights and narrow the statutory loopholes.

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[65] *See* New MBCA, *supra* note 1, § 6.30 (b)(3).

[66] *Id.* § 6.30(b)(4)-(5).

[67] *Id.* § 6.30(b)(6). It should also be noted that preemptive rights can be waived without consideration. *Id.* § 6.30(b)(2).

[68] R. Clark, Corporate Law § 17.1.4 (1986) [hereinafter Clark].

[69] *See* Katzowitz v. Sidler, 24 N.Y.2d 512, 515, 249 N.E.2d 359, 364, 301 N.Y.S.2d 470, 477 (1969)(offer of shares at 1/18 of book value without valid business purpose and with intent to dilute interest of dissenting shareholder held breach of fiduciary duty). *But cf.* Masure v. Osborne, 388 Pa. 121, 130 A.2d 157, 159 (1957)(book value not conclusive of market value; offer to plaintiff was prima facie evidence of good faith). Of course, preemptive rights often give a minority shareholder nothing more than the option of throwing his money down a bottomless well; thus other structural protections should be considered by representatives of such interests.

II. SHAREHOLDER LITIGATION

Prior Mississippi law contained only one brief statutory reference and virtually no case authority[70] on the subject of shareholders' derivative actions.[71] The only reference in the Old MBCA was section 93, which incorporated the contemporaneous ownership requirement, *i.e.*, that only one who was a shareholder at the time the challenged transaction took place could file a derivative suit.[72] The statute's silence was particularly maddening since the Mississippi Rules of Civil Procedure failed to adopt Rule 23.1 of the Federal Rules of Civil Procedure dealing with derivative actions.[73] Thus the New MBCA provisions on derivative suits bring welcome clarification to this area of Mississippi law; nonetheless it is only fair to say that the new statute leaves unanswered a number of significant questions.

Section 7.40 of the New MBCA was adopted without change from the RMA. Two prerequisites exist to maintaining a derivative action: first, as under the prior statute, the plaintiff must have been a shareholder (either of record or beneficial owner) as of the time of the challenged transaction or have received his shares by operation of law from such an owner[74]; and second, the complaint, which must be verified,[75] must allege with particularity those efforts made to obtain action by the board and their refusal to act, or why the failure to take such action should be excused.[76] Like most statutes, however, the New MBCA is unfortunately silent on the issue of what *constitutes* "demand futility," a matter on which a substantial body of often contradictory case law exists.[77] The new statute empowers the court to stay any action pending an investigation by the corporation.[78]

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[70] The sole annotated case is Liberty Sav. & Loan Ass'n v. Mitchell, 398 So. 2d 208 (Miss. 1981), which while derivative in nature involved no typical derivative action issues. Of course such a dearth of case authority on corporate issues in Mississippi is hardly unique. *See Part One*, *supra* 3, at 168.

[71] For useful general background, see CLARK, *supra* note 68, §§ 15.1 - 15.10. *See also* HENN & ALEXANDER, *supra* note 62 § 358-81.

[72] The text of the statute read as follows:

> No action shall be brought in this state by a shareholder in the right of a domestic or foreign corporation unless the plaintiff was a holder of shares or of voting trust certificates therefor at the time of the transaction of which he complains, or his shares or voting trust certificates thereafter devolved upon him by operation of law from a person who was a holder at such time.

Old MBCA, *supra* note 1, § 93. In contrast, the 1969 Model Act also provided for (1) payment to the defendant by plaintiff of reasonable expenses upon final judgment and a finding that the action was brought without reasonable cause, and (2) security for expenses. MODEL BUSINESS CORP. ACT § 49 (1969). For a detailed discussion of the contemporaneous ownership requirement, see Harbrecht, *The Contemporaneous Ownership Rule in Shareholders' Derivative Suits*, 25 UCLA L. REV. 1041 (1978).

[73] FED. R. CIV. P. 23.1. Since the federal rule would apply in the federal courts of Mississippi, it was, however, the most likely authority to be applied by analogy.

A matter of great practical significance to shareholders' attorneys is that the New MBCA, unlike the statutes of several major states,[79] makes no provision for security for expenses as a prerequisite to suit.[80] Rather, abusive or vexatious litigation is deterred by the potential for an award of the defendant's reasonable expenses, including attorneys' fees, if the court on termination (not "final judgment") finds that the suit was brought without reasonable cause.[81]

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[74] *See* New MBCA, *supra* note 1, § 7.40 (a), (e).

[75] *Id.* § 7.40(b). This requirement, imported from Fed. R. Civ. P. 23.1, has been held to require only that the plaintiff have a good faith belief in the accuracy of the allegations made, notwithstanding his failure to understand the complaint. Surowitz v. Hilton Hotels Corp., 383 U.S. 363, 373 (1966), *reh. denied*, 384 U.S. 915 (1966).

[76] *See* New MBCA, *supra* note 1, § 7.40(b). Unlike the Federal Rules, no reference is made to necessity for demand on *shareholders*, a prerequisite applied in a few jurisdictions. *See, e.g.*, Solomon & Sons Trust, Inc. v. New England Theatres Operating Corp., 93 N.E.2d 241, 248 (Mass. 1950)(if demand on officer fails, then other shareholders must be served demand). The Federal Rules require such demand only "if necessary," presumably under the substantive law of the state, and like the RMA most modern statutes adopt no such requirement. A collection of cases on the issue may be found at 2 REVISED MODEL BUSINESS CORP. ACT ANN. 741-43 (3rd ed. 1985).

[77] For a useful summary of recent cases on point, see 2 REVISED MODEL BUSINESS CORP. ACT ANN. 737-41 (3d ed. 1985).

[78] *See* New MBCA, *supra* note 1, § 7.40 (b).

[79] *See, e.g.*, CAL. CORP. CODE § 800(c)-(f) (West 1977 & Supp. 1987)(motion for security allowed if no benefit to corporation or shareholders, or if moving party was not participant in transaction); N.Y. BUS. CORP. LAW § 627 (McKinney 1986)(corporation entitled to security from plaintiffs). Currently eighteen states have such statutes. 2 REVISED MODEL BUSINESS CORP. ACT ANN. 728 (3d. 1985). On the other hand, the Illinois Business Corporation Act of 1983 makes no such provision. ILL. REV. STAT. Ch. 32, § 7.80 (1985).

[80] The drafters of the RMA took the position that such requirements discriminate unfairly against the small shareholder and are inconsistent with other types of corporate actions (*e.g.*, antitrust and class actions) that involve substantial litigation expense but impose no similar impediment. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(h)(1984).

As is true of most derivative action statutes,[82] the New MBCA provides that such suits cannot be discontinued or settled without court approval. Notice of any settlement or discontinuance, if approved, must be given to the shareholders if the court determines that their interests will be substantially affected.[83]

Perhaps the most troublesome omission in the New MBCA (as in its source, the RMA) is the failure to deal with the effect of a determination by the board of directors, or a special litigation committee appointed by the board, that the pursuit of a derivative claim is against the best interest of the corporation. Substantial variance in approach to this issue exists among recent cases. The New York rule, established by *Auerbach v. Bennett*,[84] is that the trier of fact may examine the independence, good faith, and diligence of the body recommending dismissal; beyond this, the court will not second guess the merits of the recommendation but will apply the business judgment rule. A more complex approach is taken in Delaware where, under *Zapata Corporation v. Maldonado*,[85] the court is to apply a two-step process. First, the court must review the good faith and independence of the decisionmaker and the factual bases underlying its recommendation, as to which the corporation has the burden of proof. Secondly, assuming that the corporation meets this burden, the court is to determine by applying its own business judgment whether a motion to dismiss should be granted.[86]

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[81] *See* New MBCA *supra* note 1, § 7.40 (d). The comments to the RMA state that it was deemed unnecessary to make reference to an award of attorney's fees to a successful *plaintiff*, in light of the universal recognition of this right both legislatively and judicially. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(i) (1984).

[82] *See* FED. R. CIV. P. 23.1 (court approval necessary for settlement); 2 REVISED MODEL BUSINESS CORP. ACT ANN. 727 (3d ed. 1985) (no compromise allowed without court approval).

[83] *See* New MBCA, *supra* note 1, § 7.40 (c). The statute does not prescribe who is to bear the expense of such notice (which, obviously, could be considerable); the comments to the RMA state that this is discretionary with the court. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(i) (1984).

[84] 47 N.Y. 2d 619, 633, 419 N.Y.S.2d 920, 928, 393 N.E.2d 994, 1002 (1979).

[85] 430 A.2d 779 (Del. 1981). The significance of *Zapata* has, however, been undercut by two subsequent decisions. In Aronson v. Lewis, 473 A.2d 805 (Del. 1984), the court held in effect that demand on directors should be excused only where, under the particular facts alleged by the plaintiff, a reasonable doubt exists as to the independence of the directors and the fact that the decision would be upheld by the business judgment rule. *Id.* at 814. *See* Recent Decisions, *Corporations — Derivative Action -- Demand Futility is Achieved by the Creation of a Reasonable Doubt of Directorial Disinterest Through Allegations of Factual Particularity*, 55 MISS. L.J. 181, 194 (1985)(discussing *Aronson* decision). Moreover, in Kaplan v. Wyatt, 499 A.2d 1184 (Del. 1985), the court upheld a decision by the trial judge to forego application of the second tier "independent business judgment" review of *Zapata*, emphasizing that this step was purely discretionary. 499

The drafters of the RMA simply sidestepped the issue, noting only that the law was "in state of flux" and should be allowed to develop judicially, with the possibility of an appropriate amendment to the RMA at a later date.[87] Since the resolution of this question may as a practical matter be the most significant issue in many derivative actions, I would urge the Mississippi Legislature to monitor closely the progress of the RMA in this regard and to consider the early adoption of an amendment to section 7.40 of the New MBCA to provide a clear standard for our courts to apply.

III. ORGANIC CHANGES

The New MBCA substantially alters existing laws in the area of fundamental corporate changes. Those matters will be

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A.2d at 1192.

[86] *Accord*, Joy v. North, 692 F.2d 880, 888-89 (2d Cir. 1982), *cert. denied*, 460 U.S. 1051 (1983) (business judgment rule does not apply when special litigation committee recommends dismissal of shareholder's derivative suit). For additional background see, *e.g.*, Block & Prussin, *Termination of Derivative Suits Against Directors on Business Judgment Grounds: From* Zapata *to* Aronson, 39 BUS. LAW. 1503, 1505-07 (1984) (only excused when board is extremely self-interested); Block & Prussin, *The Business Judgment Rule and Shareholder Derivative Actions: Viva* Zapata?, 37 BUS. LAW. 27, 35 (general discussion of demand requirement); Brown, *Shareholder Derivative Litigation and the Special Litigation Committee*, 43 U. PITT. L. REV. 601, 610-19 (1982)(examination of shareholder demand rule before *Aronson*); Chittur, *Ventriloquism For Corporate Directors to Terminate Shareholder Litigation: The Death of the Derivative Suit*, 75 NW. U.L. REV. 96, 98-124 (1980)(emphasis on *Auerbach* and relative positions of directors, shareholders and litigation committees); Note, *Special Litigation Committees: An Unwelcome Solution to Shareholders Demands*, 1981 U. ILL. L. REV. 485, 493-97 (examination of business judgment rule and demand requirements with thorough analysis of relevant case law).

Yet another position was taken in Miller v. Register & Tribune Syndicate, Inc., 336 N.W. 2d 709 (Iowa 1983), which refused to recognize a board-appointed committee but suggested that the court itself might appoint a committee of disinterested and experienced persons to make a recommendation on the issue. *Id.*

[87] REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 2(a) (1984).

discussed here under the classifications of amendments to the articles, sales of assets, corporate combinations, dissolution, and dissenters' rights.

A. *Amendments to the Articles and Bylaws*

In most respects, the New MBCA does not differ markedly from the provisions of the Old MBCA.[88] As under the prior law, the articles can be amended to include any provision which would have been permissible in the original articles. In lieu of an illustrative list of allowable amendments the new statute merely states that existing shareholders have no property right in any provision of the articles.[89] One innovation of the New MBCA is a list of certain essentially technical amendments which can be made by the directors without shareholder action.[90] Among these is one of significance to all Mississippi corporate practitioners: *i.e.*, an amendment to extend the corporation's duration if incorporated at a time when limited duration was required by law.[91] Now that the Mississippi Constitution has been amended to delete the ninety-nine year limitation on corporate life,[92] counsel should avail themselves of this opportunity to obtain the privilege of perpetual existence.[93]

The procedure for other article amendments is much the same as the old statute: proposal by the directors and approval by the shareholders at a meeting called for that purpose.[94] The major substantive deviation from prior law is that in the absence of a contrary provision in the articles requiring a greater vote, approval of the amendment requires only the vote of a *majority*, rather than two-thirds, of the votes of each voting group[95] entitled to vote thereon.[96] The statute actually imposes a two-fold test: if the amendment would not trigger dissenters' rights, then an affirmative majority of votes cast at a meeting where a quorum was present would suffice;[97] however, as to any voting group for whom the amendment invokes dissenters' rights, a majority of the outstanding shares of that group is also needed for approval.[98]

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[88] *See generally* Old MBCA, *supra* note 1, §§ 115-129.

[89] *See* New MBCA, *supra* note, 1, § 10.01. Thus the statute rejects the "vested rights" theory which some courts extrapolated from Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518 (1819), requiring unanimous shareholder consent for any article amendment. For background on this problem, see 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1150-51 (3d ed. 1985); HENN & ALEXANDER, *supra* note 62, § 340, at 951-55. In any event the vested rights theory was constitutionally rejected in Mississippi. *See* MISS. CONST. art. 7, § 178.

[90] *See* New MBCA, *supra* note 1, § 10.02.

[91] *Id.* § 10.02(1).

[92] 1987 Miss. Senate Concurrent Resolution No. 549, *amending* MISS. CONST. art. 7, § 178 (approved by the electorate November 10, 1987). This restriction was codified in Old MBCA, *supra* note 1, § 109. *See also Part One*, *supra* note 3, at 172 n. 27.

[93] Appropriate amendments to New MBCA § 3.02 and § 10.02 were enacted in 1988. MISS. CODE ANN. §§ 79-4-3.02, -10.02(1)(Supp. 1988).

[94] *See* New MBCA, *supra* note 1, § 10.03. The directors are called upon to "recommend" the amendment to the shareholders unless precluded from this by a conflict of

As under prior law, the concept of class voting on amendments is preserved although under the designation of votes by voting groups. This right is extended to shares with no general voting rights if the rights of such shares would be affected in one of nine enumerated ways.[99]

The amendment once approved is effected by filing articles of amendment with the Secretary of State, including prescribed information concerning the text of the amendment and the vote thereon. Consistent with the approach taken under the New MBCA generally, the formal issuance of a "certificate of amendment" is eliminated.[100] Also as under prior law, the board can restate the corporation's articles without shareholder action,[101]

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interest or "other special circumstances" which must be communicated to the shareholders. The board may also condition its submission "on any basis." *Id.* § 10.03 (b)-(c).

Prior to the issuance of shares either the board or incorporators have plenary power to amend the articles. *Id.* § 10.05.

[95] The concept of voting groups is discussed in *Part One*, *supra* note 3, at 235-36.

[96] *See* New MBCA, *supra* note 1, § 10.03(e). The statute also allows the board to alter the ordinary voting rights of shareholders by appropriately conditioning its submission to the shareholders. *Id.* § 10.03(c). *See also* Revised Model Business Corp. Act § 10.03 Official Comment (1984)(examples of conditions commonly imposed in order for amendment approval).

[97] This is the customary requirement for effective shareholder action, and treats abstentions as such, not as negative votes. *See Part One*, *supra* note 3, at 233-34 (majority of votes cast is sufficient to indicate shareholder approval).

[98] *See* New MBCA, *supra* note 1, § 10.03(e).

[99] *Id.* § 10.04.

[100] *See* New MBCA, *supra* note 1, §§ 1.25(b), 2.03; *Part One*, *supra* note 3, at 173.

[101] *See* New MBCA, *supra* note 1, § 10.07. This presupposes, of course, that the restatement contains no changes not previously approved by the shareholders; in such event shareholder approval must to that extent be obtained. *Id.* § 10.07(b).

and amendments pursuant to federal bankruptcy reorganization proceedings require neither board nor shareholder action.[102]

The provisions of the New MBCA on bylaw amendments are substantially more detailed than those of the previous statute and make at least one substantive change. Under the Old MBCA, the power to adopt or amend bylaws rested exclusively with the board absent a provision in the articles which "reserved" such power to shareholders.[103] Conversely, under the new statute the power to amend or repeal bylaws is essentially coterminous between the board and stockholders. Indeed, the New MBCA actually shifts the balance in favor of the shareholders since the board's power may be limited either by an exclusive reservation in the articles to the shareholders, or by a statement in any action by the shareholders amending or repealing a bylaw which provides that the board may not thereafter amend or repeal it.[104]

Unlike the prior law, the New MBCA deals expressly with supermajority provisions for both shareholders and directors. If authorized by the articles, shareholders may adopt or amend bylaws providing for a greater vote or quorum requirement than imposed by statute. Such action requires compliance with the greater of the existing or proposed requirements for quorum and votes. Any such bylaw cannot be adopted, amended or repealed by the board.[105] Bylaws dealing with supermajority requirements for the board are treated differently: if adopted by the shareholders, only they can amend; if by the directors, either the directors or shareholders can amend.[106]

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[102] *Id.* § 10.08.

[103] *See* Old MBCA, *supra* note 1, § 51.

[104] *See* New MBCA *supra* note 1, § 10.20. Presumably the initial bylaws would be adopted by the board absent contrary provision in the articles, although the act does not directly address this question.

While there was some split of authority, the prevailing view under statutes like the Old MBCA appeared to be that the shareholders retained inherent power to amend or repeal bylaws. *See* 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1211-12 (3d 1985)(statutory and case law background of shareholders rights to repeal or amend bylaws); HENN & ALEXANDER, *supra* note 62, § 133, at 308 & nn. 11-12 (formulation of initial bylaws is power enjoyed in different jurisdictions by incorporators, shareholders or board). The New MBCA eliminates any ambiguity on this issue.

[105] *See* New MBCA, *supra* note 1, § 10.21. Thus, for example, any attempt by shareholders to amend an existing bylaw fixing a 75% vote requirement to reduce it to 50% would itself require a 75% affirmative vote.

B. Sales of Assets

The Old MBCA followed the traditional statutory approach of requiring shareholder approval (by a two-thirds majority) of the "sale, lease, exchange, mortgage, pledge, or other disposition" of all or substantially all of a corporation's assets other than in the ordinary course of business.[107] The New MBCA changes this in three substantial respects.

First, the board is authorized to *mortgage* or otherwise encumber all or substantially all assets, either in or out of ordinary course of business, without shareholder action (unless required by the articles).[108] This is clearly a salutary change; matters of corporate financing (as opposed to the disposition of all or the bulk of a corporation's property) should appropriately be delegated to the board's discretion, subject only to the restrictions of the duties of care and loyalty.[109]

Second, transfers to a wholly-owned subsidiary are not subject to shareholder approval.[110]

The third change, consistent with the general tenor of the New MBCA, is that for those transactions subject to shareholder approval, only a majority of votes entitled to be cast, rather than two-thirds, is required absent contrary provisions in the articles.[111]

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[106] *Id.* § 10.22(a). Consistent with the previous sections, such a bylaw adopted by the shareholders may contain a provision requiring a specified vote of either shareholders or directors for any change to be effective. In addition, any board action to change a supermajority bylaw provision must also comply with the greater of the existing or proposed standard. *Id.* § 10.22(b)-(c). *See supra* text accompanying note 105.

[107] Old MBCA, *supra* note 1, § 157. The converse, expressly provided in the statute, is that no such approval was required for transfers made in the "usual and regular course of business." *Id.* § 155.

[108] *See* New MBCA, *supra* note 1, § 12.01(a)(2), (b).

[109] The requirement of shareholder approval of mortgages of property seems particularly anomalous in view of the board's unrestricted power to *borrow* without shareholder action. *See* Hodge & Perry, *supra* note 9, at 384-85 (emphasizing expense and delay caused by requiring shareholder approval of mortgages). The requirement has been deleted from the Model Act since 1962. 3 Revised Model Business Corp. Act Ann. 1321 (3d ed. 1985).

[110] *See* New MBCA, *supra* note 1, § 12.01 (a)(3).

[111] *Id.* § 12.02 (e). The procedure for authorizing sales or other dispositions not in

C. Mergers and Share Exchanges

The New MBCA makes a number of highly significant changes in current law dealing with corporate combinations: elimination of the concept of consolidations; introduction of cash mergers and share exchanges to Mississippi; and liberalization of the provisions on short-form mergers.

Chapter 11 of the New MBCA makes no mention of the consolidation procedure provided by the Old MBCA.[112] This is a rational omission: consolidations rarely occurred, since it is desired in most combination transactions that one of the constituents survive. In any event, the practical effect of a consolidation can be achieved by the simple expedient of forming a new corporation and merging the constituents into it.[113]

Of much greater practical importance is the availability of the cash merger as a means of eliminating shareholders from the combined business. Under the Old MBCA cash mergers were impermissible, since the general merger statute required that the plan of merger state the basis for "converting the shares of each merging corporation into *shares or other securities or obligations* of the surviving corporation or any other corporation."[114] Thus, with the exception of short-form mergers of subsidiaries,[115] a merger could not be used as a "cash-out" device in Mississippi. The New MBCA, however, allows the shares of the constituents to be converted as well "into cash or other property in whole or part."[116] This gives management an enormous element

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the regular course of business is essentially the same as for amendments to the articles, discussed at notes 97-99 *supra* and accompanying text. *See* New MBCA, *supra* note 1, § 12.02(f)-(g).

Two other features of the new law should be briefly noted. The first is that the board is empowered to abandon any transaction once approved without further shareholder action (without, of course, prejudicing any contractual rights of third parties). The other is that transactions which involve a transfer of assets but which actually serve the purpose of a distribution (*e.g.*, a "spin-off" or other divisive reorganization) are governed by the rules on distributions. *Id.* § 12.02(f)-(g).

[112] *See* Old MBCA, *supra* note 1, § 143. In a traditional consolidation, two or more corporations would combine to form a third, new corporation, *i.e.*, neither of the combining corporations would survive.

[113] REVISED MODEL BUSINESS CORP. ACT Ch. 11, Introductory Comment (1984).

[114] *See* Old MBCA, *supra* note 1, § 141(c)(emphasis added).

[115] *Id.* § 149; *see infra* notes 128-29 and accompanying text.

[116] *See* New MBCA, *supra* note 1, § 11.01(b)(3). Cash mergers were added to the

of flexibility in the merger process. However, it likewise injects into Mississippi law the highly volatile issue of whether a merger intended to freeze out minority shareholders may constitute a breach of fiduciary obligation by those in control.[117] Since the statute permits this procedure it is obviously not automatically voidable; the appropriate standard of review is of course not addressed by the statute and will be a matter with which Mississippi courts will ultimately grapple.

Even more innovative is the New MBCA provision for share exchanges. This procedure, unknown to common law and traditional statutes, was added to the Model Act in 1976 in order to provide a direct means whereby a corporation being acquired does not disappear but becomes a subsidiary of the acquiring corporation.[118] Under the Old MBCA this result could be accomplished only by the so-called reverse triangular merger: the acquiring corporation forms a subsidiary in which it places securities or cash; the subsidiary then merges with the target corporation, which receives securities or cash of the parent for its shares and ceases to exist.[119] The Old MBCA authorized the

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Model Act in the 1969 revision. *See* 2 Model Business Corp. Act Ann. § 71(c) (2d ed. 1971) (examines allowance of cashout mergers); Garrett, *Merger Meets the Common Law*, 63 Tex. L. Rev. 1509, 1515 (1985) [hereinafter Garrett] (discussion of impact of allowing cash out mergers).

[117] A useful summary of the recent cases (mostly from Delaware) on this issue is found at 3 Revised Model Business Corp. Act. Ann. 1261-67 (3d ed. 1985). For further background, see Herzel & Colling, *Establishing Procedural Fairness in Squeeze-Out Mergers After* Weinberger v. UOP, 39 Bus. Law. 1525 (1984) (discussion of current state of procedural fairness standard); Berger & Allinham, *A New Light on Cash - Out Mergers:* Weinberger *Eclipses* Singer, 39 Bus. Law. 1 (1984)(examination of evolution of courts' treatment of mergers); Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware Corporation Law*, 76 Nw. U.L. Rev. 913 (1982)(recent Delaware cases expand ability of dissident shareholders to challenge mergers); Greene & Junewicz, *A Reappraisal of Current Regulation of Mergers and Acquisitions*, 132 U. Pa. L. Rev. 647 (1984)(general review of statutory and case law limitations); Comment, *Freezeouts Under the 1983 Illinois Business Corporation Act: The Need for Protection of Minority Shareholders From "Going Private" Transactions*, 1985 U. Ill. L. Rev. 679 (1985) (limited protection available to minority shareholders).

[118] *See* Garrett, *supra* note 116, at 1516. The equivalent of a share exchange has, of course, always been possible assuming the unanimous consent of the shareholders of the target corporation; the innovation of the new procedure is to permit this, like a merger, in the absence of unanimity.

[119] For a somewhat more detailed description, see Norton, *The Acquisition Process and the Closely-Held Corporation: Selected Legal Aspects,* 36 Mercer L. Rev. 567,577-

reverse triangular merger by permitting conversion of shares of the target into securities of "the surviving corporation or *any other corporation*."[120]

Section 11.02 of the New MBCA again modernizes Mississippi law by providing a direct means to the same result: a plan of share exchange, whereby the shares of the target are exchanged for securities of the acquiring or any other corporation, or cash or other property.[121] The exchange is subject to all of the procedural safeguards, including dissenters' rights, as a merger.[122]

Procedurally, the plan of merger or share exchange, once adopted, is submitted either to the shareholders of both corporations (merger) or the acquired corporation (share exchange)[123] for approval.[124] Essentially the same steps for approval are required as apply to amendments of the articles, including majority vote rather than two-thirds as under the Old MBCA, and voting by voting groups under some circumstances.[125]

The New MBCA diverges from prior law in specifying limited circumstances in which the shareholders of the surviving corporation need not approve a merger.[126] In effect it is a *de minimis* exception for instances in which the merger does not significantly affect the survivor's shareholders; *e.g.*, the articles of the survivor are not substantively changed, the shareholders of the survivor hold the identical number of shares as before the

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78 (1985) [hereinafter Norton] (discussion of triangular mergers).

[120] Old MBCA, *supra* note 1, § 141(c)(emphasis added). As previously noted, however, cash was not a permissible item of exchange. *See supra* notes 114-15 and accompanying text.

[121] *See* New MBCA, *supra* note 1, § 11.02 (b)(3).

[122] The statute does not, of course, preclude the acquisition of another corporation's shares through a voluntary tender offer or other consensual transaction. *Id.* § 11.02(d).

For additional background on share exchanges, see Norton, *supra* note 119, at 581-82.

[123] Therein lies, obviously, one of the advantages of the share exchange: since the interests of the shareholders of the *acquiring* corporations are not directly affected, there is no necessity for their approval of the acquisition.

[124] *See* New MBCA, *supra* note 1, § 11.03 (outlining procedure for approval of merger or share exchange).

[125] *Id.* § 11.03(e)-(f). *See supra* notes 94-99 and accompanying text (procedure for article amendments).

[126] *See* New MBCA, *supra* note 1, § 11.03(g).

merger, and the shares issued as part of the merger do not increase the outstanding voting and participating shares of the survivor by more than twenty percent. While this avoids the necessity of a shareholder meeting for the survivor, it is probably of limited practical significance. A shareholder's meeting can, in any event, be avoided by a three-step transaction: the survivor can create a wholly-owned subsidiary; it can cause the subsidiary and target to merge; then, if desired, it can effect a short-form merger of the subsidiary without a shareholder vote.[127]

As under the Old MBCA,[128] the new statute provides for the short-form merger of a substantially owned subsidiary without any shareholder action. The major change effected by the New MBCA is that the necessary ownership threshold is now ninety, rather than ninety-five, percent.[129]

After approval of a plan of merger or share exchange by the shareholders (or by the directors alone if shareholder action is unnecessary) articles of merger or share exchange are filed with the Secretary of State.[130] Consistent with the general approach of the New MBCA, the articles are self-effectuating and no certificate of merger is issued by the Secretary.

The provisions of the New MBCA involving the effects of a merger or share exchange, and addressing combinations between domestic and foreign corporations, do not materially differ from the prior statute.[131]

D. Dissolution

The New MBCA provisions on dissolution do not, for the most part, differ significantly from the old statute.[132] In a few respects, however, the new act makes important changes in the prior law.

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[127] *See* Murphy, *The New Virginia Stock Corporation Act: A Primer*, 20 U. RICH. L. REV. 67, 122 (1985) [hereinafter Murphy] (analyzing effect of not having shareholders meeting on merger or share exchange).

[128] *See* Old MBCA, *supra* note 1, § 149.

[129] *See* New MBCA, *supra* note 1, § 11.04.

[130] *Id.* § 11.05.

[131] *Compare* Old MBCA, *supra* note 1, §§ 151, 153, *with* New MBCA, *supra* note 1, §§ 11.06, 11.07.

[132] *E.g.*, plenary authority to effect a dissolution is still granted to incorporators or directors of a corporation which has not issued shares nor commenced business. *Compare* Old MBCA, *supra* note 1, § 163, *with* New MBCA, *supra* note 1, § 14.01. In addition, the provisions on judicial dissolution are not materially different. *Compare* Old

Regarding voluntary dissolution, the New MBCA alters present law in two ways. First, the New MBCA requires action of both directors and shareholder to effect dissolution of an organized corporation;[133] the former provision for dissolution by unanimous written consent of shareholders is now eliminated.[134] Thus, the formality of a board resolution will have to be observed in any dissolution of a corporation which has begun business or issued stock. Second, consistent with the preceding discussions, dissolution now requires the consent of only a bare majority of shares entitled to vote in the absence of a provision in the articles increasing the threshold;[135] the prior act, of course, required a two-thirds affirmative vote.[136]

Procedurally, the separate steps of filing an intent to dissolve, followed by winding up of the corporate affairs and the filing of formal articles of dissolution,[137] are eliminated. Rather, after dissolution, articles of dissolution will now be filed with the Secretary of State, and the corporation will be deemed dissolved as of their effective date.[138] This, in turn, triggers the winding up and liquidation of its business and affairs, the procedure for which is outlined in section 14.05.[139] The most significant procedural changes are in the area of liabilities. More detail is now included involving notice to known creditors; this must be done in writing and allow not less than 120 days for the filing of a claim. Any such claim will be barred if the claimant fails to respond or to file an action to enforce a claim within 90 days of its

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MBCA, *supra* note 1, §§ 193, 195, *with* New MBCA, *supra* note 1, §§ 14.30, 14.31.

[133] *See* New MBCA, *supra* note 1, § 14.02.

[134] *See* Old MBCA, *supra* note 1, § 165.

[135] *See* New MBCA, *supra* note 1, § 14.02(e). The board can also increase the required vote by so conditioning its submission to shareholders. *Id.* § 14.02(c).

[136] *See* Old MBCA, *supra* note 1, § 167(c).

[137] *Id.* §§ 167(d), 169-173, 183-85.

[138] *See* New MBCA, *supra* note 1, § 14.03.

[139] *Id.* § 14.05. This includes the collection of assets, disposition of all property not to be distributed to shareholders, payment of outstanding liabilities, distribution of the remaining property to shareholders, and such other acts "necessary to wind up and liquidate its business and affairs." *Id.* § 14.05(a). The statute also outlines those matters not affected by dissolution per se, including title to the corporation's property. *Id.* § 14.05(b).

rejection by the corporation.[140]

Perhaps more significant is the New MBCA's treatment of unknown claims. The new act allows the corporation to publish notice in a newspaper of general circulation providing a procedure for the filing of unknown or contingent claims, and a statement that any such claim will be barred if an action to enforce is not filed within five years.[141] This provision now provides, in effect, a uniform statute of limitations for unknown or contingent claims.[142] Moreover, it effectively overrules *Naugher v. Fox River Tractor Company*.[143] In that case, the court held under section 209 of the Old MBCA that while a product liability action against a dissolved corporation *arose* at the time of manufacture, it would not be barred until six years from the date of *injury*,[144] thereby creating virtually unlimited exposure for such claims.[145]

In the area of involuntary dissolution, two important changes are made by the New MBCA. The first is an entirely new set of provisions for administrative dissolution. The grounds for dissolution by the Secretary of State now include failure to pay franchise taxes or penalties; failure to file an annual report; failure to maintain a registered office, or agent, or to notify the Secretary of State of changes thereto; and the expiration of a corporation's duration.[146] Given the largely ministerial nature of such vices, however, the statute also provides a fairly simple procedure for reinstatement upon cure, together with a right of judicial appeal from any denial of reinstatement.[147]

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[140] *Id.* § 14.06. The prior statute required that written notice be sent but did not specify any sanction for failure to respond. Old MBCA, *supra* note 1, § 173(a). Rather, such claims survived for the period of the applicable statute of limitations. *Id.* § 209.

[141] *See* New MBCA, *supra* note 1, § 14.07. This would have the effect, after the five year period, of barring known claimants not receiving notice; claimants who filed a claim but were not paid; and contingent claims or those based on events occurring after dissolution. *Id.* § 14.07. If an action is timely filed, the corporation (to the extent of the assets it has retained) or shareholders (for their pro rata share or the amount of assets distributed to them, whichever is less) can be held liable. *Id.* § 14.07(d).

[142] *Id.* § 14.07(c). Under the Old MBCA the limitation period varied according to the nature of the claim. *See supra* note 140.

[143] 446 F.Supp. 1281 (N.D. Miss. 1977).

[144] *Id.* at 1282-83 (analyzing Mississippi's general statute of limitations).

[145] *Id.* at 1283. *See also* New MBCA, *supra* note 1, § 14.07(c)(3). Presuming that the requisite notice is published, any such claim would either be "contingent" (if the injury was incurred before dissolution) or "based on an event occurring after the effective date of dissolution" (if the injury was incurred at that time), and thus would be barred by the passage of five years under New MBCA § 14.07(c)(3).

[146] *See* New MBCA, *supra* note 1, § 14.20. Under the MBCA certain grounds would

The other principal innovation of the New MBCA is the power granted to a court conducting a proceeding for judicial dissolution to appoint a custodian to manage its business as an alternative to a liquidating receiver.[148] Although the statute is silent as to those factors to be weighed by the court in determining whether a custodianship would be appropriate, presumably it is intended as a less drastic alternative to liquidation and a device to effect a resolution of the internal difficulties which gave rise to the proceeding.[149] If nothing else, since the statute allows the delegation of "all powers of the corporation through or in place of its board of directors or officers" to the custodian,[150] this may provide the requisite impetus to a buy-out of complaining shareholders or other voluntary settlement of the underlying controversy. If appropriate, the court may also convert a custodianship to a receivership, and vice versa.[151]

E. Dissenters' Rights

The traditional approach to dissenters' rights, as embodied in the Old MBCA,[152] has been the subject of criticism both by shareholder and management interests. For the shareholder who

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have justified involuntary judicial dissolution through an action filed by the Attorney General, or suspension of the corporation's charter by the Secretary of State. Old MBCA, *supra* note 1, §§ 187-89. As a practical matter, however, few such actions were pursued by the Attorney General, and the sanction of suspension (although theoretically carrying with it denial of the privilege of doing business) often failed to provide the requisite impetus for corrective action by a recalcitrant corporation's managers. The device of administrative dissolution is both more economically efficient and, at the same time, may carry a connotation of seriousness that mere "suspension" did not.

For the procedure to be followed by the Secretary, including the requisite notice periods, see New MBCA, *supra* note 1, § 14.21.

[147] *See* New MBCA, *supra* note 1, § 14.22-14.23.

[148] *Id.* § 14.32(a). The Old MBCA recognized only the receivership concept. Old MBCA, *supra* note 1, § 195-97.

[149] *See* REVISED MODEL BUSINESS CORP. ACT. § 14.32 Official Comment (1984).

[150] New MBCA, *supra* note 1, § 14.32 (c)(2).

[151] *Id.* § 14.32(d). For other matters involving the procedure for judicial dissolution, see *id.* §§ 14.31, 14.33.

[152] *See* Old MBCA, *supra* note 1, §§ 159, 161.

objected to one of the enumerated transactions that triggered dissenters' rights,[153] this dissatisfaction was eminently understandable: the procedure for asserting them was highly complex, thus subjecting the dissenter to the risk of losing his rights by technical noncompliance,[154] and in any event involved the expense of a court action to determine the "fair value" of his shares if the parties could not agree.[155] In turn, that complexity and expense created from management's perspective an inherent potential for nuisance litigation motivated by settlement value, or demands based upon unrealistic visions of a stock's worth.[156] Finally, the generally worded definition of "fair value" in the statute offered no guidance as to how it should be determined.[157]

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[153] *Id.* § 159. Under the Old MBCA these included only (1) mergers and consolidations and (2) the sale or exchange of all or substantially all of the corporation's assets other than in the ordinary course of business. *Id.*

[154] In brief, the Old MBCA demanded the following: (1) written objection by the shareholder prior to or at the meeting where action was to be taken; (2) the shareholder had to vote against the action; (3) the shareholder had to make written demand for payment of the "fair value" of his shares within 10 days of the vote (15 days if a short-form merger); (4) if within 30 days thereafter the corporation and shareholder could not agree on such fair value, then the corporation could, within 60 days of the transaction complained of, file an action to determine the fair value of his shares; (5) if the corporation failed to bring such an action within the 60 day period, then any shareholder could commence the action. In all events, the shareholder was required to deposit his share certificates with the corporation within 20 days of his initial demand; failure to do so would result in the termination of his rights unless his failure was excused by a court "for good and sufficient cause." *Id.* § 161.

Of course the corporation and shareholder might agree upon the question of valuation, in which instance payment was to be made within 90 days of the transaction. *Id.*

[155] Committee on Corporate Laws, *Changes in the Model Business Corporation Act Affecting Dissenters' Rights*, 32 BUS. LAW. 1855, 1856 (1977)[hereinafter *Dissenters' Rights*]. Under the Old MBCA, the expense of a valuation proceeding was borne by the corporation unless the court found that the refusal by the shareholder to accept the corporation's offer was "arbitrary or vexatious or not in good faith," in which instance all or part of the expense could be taxed to the shareholder. In all events, each party had to pay his own attorneys' fees. Old MBCA, *supra* note 1, § 161.

[156] *See Dissenters' Rights*, *supra* note 155, at 1856.

[157] The most commonly accepted procedure is the so-called "Delaware block" method where the three elements of value, *i.e.*, assets, market value, and earnings, are assigned a designated weight, and the amounts thereby determined are added to reach a per share value. Norton, *supra* note 119, at 585. A recent Mississippi case suggests an emphasis on historical earnings as the most significant component in the closely-held business. Hernando Bank v. Huff, 796 F.2d 803 (5th Cir. 1986). For general background see, *e.g.*, Comment, *Valuation of Shares in a Closely Held Corporation*, 47 MISS. L.J. 715 (1976)(examination of factors used in determining fair share value); Note, *The Dissent-*

The drafters of the Model Act fundamentally restructured the concept of dissenters' rights in 1977 to strike a more equitable balance of competing policies.[158] The New MBCA adopts the Model Act approach, which broadly seeks to encourage the parties to compromise their differences privately, with judicial appraisal available only as a matter of last resort.[159] Technically the statute changes prior law in several significant respects.

Initially, the New MBCA expands the scope of dissenters' rights over the limitations previously imposed.[160] Dissenters' rights now apply to mergers as to which the dissenter has a right to vote; short-form mergers where the dissenter owns shares of the corporation which does not survive; share exchanges if the dissenter is a shareholder of the acquired corporation and has a right to vote on the plan; sales or exchanges of all or substantially all assets not in the ordinary course of business (excluding judicial sales and liquidation sales in which the proceeds are distributed to shareholders within one year); amendments to the articles that affect a dissenter's shares in any of five enumerated ways; and other transactions as to which the articles, bylaws, or board resolution provide dissenters' rights.[161] In addition, dissenters' rights are now extended to beneficial shareholders as well as shareholders of record.[162]

In another respect, however, the New MBCA is more restrictive than the old law. Dissenters' rights are now made the exclusive remedy of a shareholder to whom the rights accrue un-

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ing Shareholder's Appraisal Remedy, 30 OKLA. L. REV. 629 (1977)(general discussion of relevant factors in determining value of shares held by dissenting shareholder).

[158] *See Dissenters' Rights, supra* note 155, at 1856-57.

[159] REVISED MODEL BUSINESS CORP ACT Ch. 13 Introductory Comment (1984).

[160] *See supra* note 153.

[161] *See* New MBCA, *supra* note 1, § 13.02. The inclusion of article amendments remedies perhaps the most glaring deficiency of the Old MBCA, under which, for example, shares could be stripped of preferences, redemption rights, or preemptive rights without a right to dissent. *Cf. id.* § 13.02 (4).

[162] *Compare* Old MBCA, *supra* note 1, § 3(g)(defining shareholder as a "holder of record") with New MBCA, *supra* note 1, § 13.01 (7)(defining shareholder as "the record shareholder or the beneficial shareholder" for purposes of dissenters' rights provisions). A 1988 amendment makes it clear that "beneficial shareholders" include the beneficial owners of shares held by a voting trust. MISS. CODE ANN. § 79-4-13.01(6) (Supp. 1988). For the mechanics of the assertion of dissenters' right by a beneficial owner, see *id.* § 13.03(b).

less the proposed action is "unlawful or fraudulent" as to either the shareholder or corporation.[163] This aspect of the law is likely to engender controversy. The rationale advanced by the drafters of the RMA is that so long as a majority of shareholders approve a transaction, their decision should prevail against a minority interest which deems it unwise or disadvantageous even if a court should side with the minority.[164] While logic supports this proposition, it is defensible only if one assumes that the minority shareholder is assured of a fair payment for his shares. Although the question is certainly debatable, on balance by adopting the broad unlawfulness or fraud exception the statute is probably sufficiently flexible to alleviate any concerns that it unduly favors majority interests.[165]

While the overall goal of the New MBCA is to make the assertion of dissenters' rights a more practicable remedy, it should be noted that the enforcement procedure has not by any means been significantly simplified. The procedure is outlined in sections 13.20 through 13.28. Initially, if a meeting is called to consider an action triggering dissenters' rights, the notice of the meeting must state this and be accompanied by a copy of Chapter 13 of the New MBCA. If the transaction does not require shareholder approval then the corporation must notify the shareholders of the action and send a dissenters' notice described in section 13.22.[166]

If the action requires a shareholder vote then the shareholder must give written notice of his intent to exercise dissenters' rights before the vote is taken and either vote against the action or abstain. Failure to do so results in the forfeiture of his right to payment under Chapter 13.[167] Thus, as under prior law, strict attention to question of technical compliance is required.

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[163] *See* New MBCA, *supra* note 1, § 13.02(b). Consistent with this approach, the new statute also forecloses the former right of a shareholder to dissent only as to part of his shares. *See* Old MBCA, *supra* note 1, § 159. Such action is now permissible only in those instances where the shareholder acts as a nominee for several beneficial shareholders, some of whom do not wish to dissent. New MBCA, *supra* note 1, § 13.03(a).

[164] REVISED MODEL BUSINESS CORP. ACT § 13.02 Official Comment 2 (1984).

[165] While eschewing any attempt at comprehensiveness, the RMA suggests actions in violation of legal voting provisions, in violation of the articles, and those involving deception or breach of fiduciary duties as examples of transactions not protected from judicial intervention. *Id.* It should be noted that the clear trend is to make dissenters' rights exclusive. For a collection of statutes and cases on point, see 3 MODEL BUSINESS CORP. ACT ANN. 1372, 1374.2-1377 (Supp. 1987).

[166] *See* New MBCA, *supra* note 1, § 13.20.

Following the meeting and within 10 days, the corporation must send a "dissenters' notice" to all shareholders who properly asserted dissenters' rights. The notice must *inter alia* state the time and place for demanding payment and tendering shares, supply a form for demanding payment, and set a date not less than 30 nor more than 60 days from the date of the notice by which the demand for payment must be received.[168] Thereafter the onus is upon the recipient to demand payment and deposit his shares pursuant to the terms of the notice; again his failure to comply will result in the loss of his rights under Chapter 13.[169]

Within 60 days after the deadline for demanding payment and depositing shares,[170] the corporation is required to pay each complying dissenter the amount estimated by the corporation to be the fair value of his shares with accrued interest. The corporation must transmit with the payment financial statements for a fiscal year ended not more than 16 months prior to payment, an explanation of the method used to determine fair value and to calculate interest, a statement of the dissenters' rights under section 13.28 if he is dissatisfied with the offer, and yet another copy of Chapter 13.[171]

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[167] *Id.* § 13.21.

[168] Id. § 13.22. The notice must also advise holders of uncertified shares of any restrictions that will be placed upon transfer after demand, and include a copy of Chapter 13. Of course, as to the latter one may legitimately question the layperson's ability to understand such a complex statute, but clearly no harm is done by its inclusion.

[169] *Id.* § 12.23(a), (c). The statute makes it clear, however, that the demanding shareholder retains all other rights as a shareholder until his rights are cancelled or modified by effectuation of the transaction. *Id.* § 13.23(b).

[170] *See id.* § 13.26(a).

[171] *Id.* § 13.25. Similar to the Old MBCA, the new act defines "fair value" as "the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable." *Id.* § 13.01(3). The drafters of the RMA candidly admit, however, that this offers little guidance (other than timing) as to the methodology to be employed in calculating "fair value." REVISED MODEL BUSINESS CORP. ACT § 13.01 Official Comment 3 (1984). *See supra* note 157 and accompanying text.

If the corporation does not make the required payment within the 60 day limit it

Should a shareholder be dissatisfied with the amount tendered, or if payment is not made by the corporation within the 60 day period, under section 13.28 the dissenter may within 30 days after payment is made transmit to the corporation his own estimate of the fair value of his shares together with a demand for that amount. Failure to do so waives his right to such demand.[172]

Only if the parties fail to agree upon fair value after the exhaustion of this procedure can they resort to judicial appraisal. The corporation must within 60 days after receiving demand under section 13.28 file an action to determine the fair value of the dissenters' shares if no agreement is reached. Corporate counsel should note well the importance of timing; failure to file the action obligates the corporation to pay the demanded sum.[173] All dissenters whose claims are unresolved are to be joined, and the court is empowered to appoint and define the responsibilities of appraisers. The dissenters are to receive judgment for the amount, if any, by which the court-determined fair value, plus interest, exceeds the corporation's payment.[174]

Interestingly, the New MBCA is somewhat ambiguous as to what a dissatisfied dissenter should do with the payment he receives from the corporation if he intends to make a supplemental demand under section 13.28. The only light that the RMA comments shed upon the issue is that the statute is meant to force the corporation to pay without taking advantage of any delay pending final agreement, thereby eliminating the leverage that dilatory tactics would provide. Likewise, the shareholder is to be afforded immediate use of the amount tendered.[175] The statutory formulation of judicial relief, *i.e.*, the difference be-

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must return the certificates to the shareholder; if thereafter the transaction complained of is consummated, the above procedure of notice and demand must be repeated. New MBCA, *supra*, note 1, § 13.26.

[172] *See* New MBCA, *supra* note 1, § 13.28. The right to make his own estimate and demand is also provided if the corporation does not consummate the transaction of which he complains, but fails to return his certificates or release transfer restrictions on uncertificated shares under section 13.26(a).

[173] *Id.* § 13.03(a). Under the Old MBCA no such sanction existed; rather it only freed the dissenter to file the action. *See supra* note 154.

[174] *Id.* § 13.30(c)-(e).

[175] Revised Model Business Corp. Act § 13.25 Official Comment (1984).

tween fair value and the corporation's payment, suggests that the shareholder should be free to avail himself immediately of the initial payment without risking a waiver of his rights. Moreover, the statutory right to make the supplemental demand should foreclose the addition of any "accord and satisfaction" language to the corporation's check. Nonetheless, an explicit statement of the shareholder's right to use the initial payment pending resolution of his supplemental demand would be a desirable amendment to the new MBCA; absent this the prudent dissenter negotiating a check tendered pursuant to section 13.25 might well include a reservation of rights in his endorsement.[176]

While the costs of the judicial proceeding, including expenses incurred by appraisers, are ordinarily borne by the corporation, the statute grants broad discretion to the court to tax such expenses to dissenters if it deems them to have acted arbitrarily, vexatiously or in bad faith. Likewise, attorneys' fees can be imposed upon either the corporation or dissenters if the court finds that either party did not comply in good faith with the provisions of Chapter 13.[177]

Only experience will show whether the new act accomplishes the avowed goal of rendering dissenters' rights a more realistic remedy. While the New MBCA is far clearer and better organized than its predecessor, in frankness it has not simplified the procedure for exercising dissenters' rights to any appreciable extent. The same pitfalls exist as before for the shareholder who lacks diligence in pursuing his rights, and it would be foolhardy indeed for a dissenter not to engage the services of competent counsel. On the other hand, procedural aspects aside, the statutory incentives for negotiated settlement — particularly mandatory early payment by the corporation (as opposed to a simple offer) and the right for dissenters to make a supplemental demand — seem real and substantial. In this regard the New MBCA represents a positive step towards more satisfactory resolution of these disputes.

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[176] *Cf.* MISS. CODE ANN. § 75-1-207 (1972)(UCC provision for reservation or preservation of rights).

[177] *See* New MBCA, *supra* note 1, § 13.31 (a), (b). This discretion also extends to requiring that some dissenters contribute to the attorney's fees of other dissenters if they substantially benefitted from the services performed by the latter. *Id.* § 13.31(c).

IV. Close Corporations

A. Introduction

The overwhelming majority of Mississippi corporations are closely held, and surely there is no debate that such entities are different, not just in degree but in kind, from the public corporation. One of the dominant themes in corporate scholarship and legislation, at least since the mid-1950's, has been the attempt to respond effectively to problems peculiar to the close corporation.[178] General corporation statutes have commonly adapted to meet some of the needs of close corporations, but traditional statutes such as the Old MBCA have proven deficient in many particulars. Moreover, while judicial recognition of the special nature of the close corporation has increased in recent years,[179] this trend has not been universal, particularly in instances where shareholder control over board discretion has been involved.[180] Clearly, additional statutory "safe harbors" are desirable to facilitate effective planning where variations of the statutory model are appropriate. Paradoxically, though, the Old MBCA reflected a large corporation orientation.[181]

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[178] Some common examples are (1) supermajority vote and quorum provisions; (2) provision for informal shareholder or director action by unanimous consent or conference telephone call; (3) broad powers of delegation to board committees; (4) broad power to restrict transfers of shares; (5) authorization of voting trusts; (6) provisions for one incorporator; (7) provision for fewer than three directors; and (8) broader provisions for dissolution, *e.g.*, by unanimous shareholder consent. Miller, *Illinois Close Corporations: Analysis of the New Act*, 27 DEPAUL L. REV. 587, 601 (1978). Of these it is noteworthy that the Old MBCA had no provision as to (4), (6), or (7), and as to (2) did not recognize conference telephone calls as a permissible means of shareholder or director action. Old MBCA, *supra* note 1.

[179] Perhaps the best-known example is Donahue v. Rodd Electrotype Co., 328 N.E. 2d 505, 515-16 (Mass. 1975), which states that shareholders in a close corporation owe one another substantially the same fiduciary duties as partners.

The Mississippi Supreme Court has followed this trend in an important recent decision involving issues of authority. In Baxter Porter & Sons Well Servicing Co. v. Venture Oil Corp., 488 So. 2d 793, 796 (Miss. 1986), the court equated the authority of a shareholder, executive officer and director of a close corporation to that of a partner in a partnership as to matters that constitute carrying on the usual business of the corporation. *Cf.* MISS. CODE ANN. § 79-12-17(a)(Supp. 1987)(authority of partnership as agent for partnership). While the result reached in *Baxter Porter, i.e.*, binding the corporation to acts undertaken by such a person without formal board approval, is not surprising, the court's candid admission that the pristine rules of agency simply should not apply in the close corporation setting is a praiseworthy move towards more honest and realistic decisionmaking in this area.

[180] *See infra* notes 199-201 and accompanying text.

The recent response to this need has been broadly twofold: in some states, the enaction of special "close corporation" statutes either as a supplement or alternative to the general corporation statute;[182] in others, the addition of special provisions of particular significance to the close corporation to a general corporation statute. The RMA, from which the New MBCA was derived, takes the latter approach.[183] I believe this is fundamentally sound,[184] and certainly the New MBCA is a vast improvement over its predecessor. Nonetheless, there remain some problem areas which the new act does not address, and to which the legislature should give close attention in the future. Before dealing with those issues, however, I will discuss the major innovations of the New MBCA.

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[181] *See Part One*, *supra* note 3, at 170 n. 15.

[182] These statutes generally adopt criteria for classification as a statutory close corporation, and a set of special rules applicable only to such corporations. For an extensive discussion of such statutes, see 1 H. O'NEAL, CLOSE CORPORATIONS § 1.14b (2d ed. 1971 & Supp. 1987) [hereinafter O'NEAL]. A list of states with integrated close corporation provisions can be found at 4 MODEL BUSINESS CORP. ACT ANN. 1868 (3d ed. Supp. 1987).

[183] In 1981, the ABA Committee on Corporate Laws first promulgated a proposed supplement to the Model Act, presenting an integrated close corporation statute. *See* Committee on Corporate Laws, *Statutory Close Corporation Supplement to the Model Business Corporation Act*, 37 BUS. LAW. 269 (1981)(results of committee's work). The Supplement was formally adopted with amendments in 1983. *See* Committee on Corporate Laws, *Statutory Close Corporation Supplement to the Model Business Corporation Act*, 38 BUS. LAW. 1031 (1983)(detailing adoption of amendments). The current text can be found at 4 MODEL BUSINESS CORP. ACT ANN. 1803-1862 (3d ed. 1985). The Supplement was, however, not proposed by the Task Force as a part of the Business Law Reform legislative package. For a summary and critique of the Supplement, see Kessler, *The ABA Close Corporation Statute*, 36 MERCER L. REV. 661 (1985).

[184] Author's Note: The debate over the desirability of integrated close corporation statutes is of long standing, and I will make no effort to resolve it here. A useful summary of the arguments pro and con is found in O'NEAL, *supra* note 182, §§ 1.13-1.14(c). I have been convinced by those who argue that a well-drafted general incorporation act with provisions that respond to basic close corporation issues offers sufficient flexibility to planners without the necessity for the creation of an arbitrarily defined "statutory close corporation." A well-reasoned statement of this proposition is Karjala, *A Second Look at Special Close Corporation Legislation*, 58 TEX. L. REV. 1207 (1980)[hereinafter Karjala]. It is noteworthy that Florida, which adopted one of the pioneering integrated close corporation acts, subsequently repealed it.

Perhaps more germane is whether it is rational to maintain artificial demarcations between the partnership and corporation in the small business setting. The ultimate goal in this area more appropriately might be a new unified small business form combining the most desirable features of the laws of partnerships and corporations. For a discussion of this question, see Haynsworth, *The Need for a Unified Small Business Legal Structure*, 33 BUS. LAW. 849 (1978). This, however, goes beyond the scope of the present article.

B. Share Transfer Restrictions.

The Old MBCA did not directly validate restrictions on the transfer of shares, thus leaving the efficacy of such devices to be determined by judicial precedent.[185] The New MBCA greatly improves the law by explicitly authorizing share transfer restrictions and delineating the types of restrictions which may be permissible.

Under section 6.27, transfer restrictions are authorized to maintain a corporation's status where determined by the number of its shareholders (*e.g.*, an election under Subchapter S of the Internal Revenue Code), to preserve a securities law exemption, or for "any other reasonable purpose."[186] The types of restrictions authorized by the statute are (1) rights of first refusal, (2) obligations to purchase restricted shares, presumably upon the occurrence of some contingency, (3) consent provisions if not "manifestly unreasonable," and (4) disqualifications of certain purchasers (*e.g.*, competitors) if not "manifestly unreasonable."[187]

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[185] The leading case was Fayard v. Fayard, 293 So. 2d 421 (1974), which adopted the rule that transfer restrictions in close corporations would be sustained if determined to be "reasonable in the light of the relevant circumstances." *Id.* at 423. The court went on to enumerate the factors to be considered as including: (1) size of the corporation, (2) degree of the restraint, (3) duration of the restraint, (4) method of fixing share value, (5) relation of the restraint to corporate objectives, (6) the threat posed by a hostile shareholder, and (7) the likelihood that the restriction would serve the corporation's best interest. Applying this test the court held that a restriction in a family corporation requiring consent of all shareholders to any transfer was valid as to transfers outside of the family but invalid as to intrafamily transactions. *Id.* at 424. One might, however, question the court's premise that transfers to third parties would be inherently more disruptive and prone to create disharmony than transfers to other family members.

[186] *See* New MBCA, *supra* note 1, 6.27(c). Of course this still leaves the definition of such "reasonable purposes" ultimately in the hands of courts, but there is a substantial body of caselaw nationwide from which guidance can be drawn. For a collection and summary of cases, see 1 MODEL BUSINESS CORP. ACT ANN. 432-443 (3d ed. Supp. 1987).

[187] *See* New MBCA, *supra* note 1, § 6.27(c). Consent restrictions have been particularly risky at common law, despite the *Fayard* court's acceptance in the family corpora-

The usefulness of share transfer restrictions, both for controlling entry to and exit from a business venture and for providing liquidity of investment, are well known and need not be repeated here. In light of the preceding discussion of dissenters' rights, however, one might note a particular advantage that such provisions can serve in the closely-held corporation as a contractual alternative to Chapter 13. A provision mandating the buyout of a minority interest upon the occurrence of some condition can not only be extended beyond the statutory events triggering dissenters' rights, but also has the advantage of allowing the parties to fix the price of shares in advance of any dispute and thereby avoid the possible necessity of judicial appraisal.

The statute permits transfer restrictions in either the articles, bylaws or separate contracts; of course those owning shares prior to the adoption of a restriction are bound only if they vote for it or become parties to the contract. In order to be enforceable against third party transferees the restriction must be conspicuously legended on the front or back of a certificate.[188]

C. *Shareholders' Agreements.*

While the Old MBCA had no provisions on shareholders' agreements other than formal voting trusts,[189] the common law generally recognized the validity of agreements among shareholders dictating how they would vote their shares.[190] Rather, the problems encountered with so-called "pooling agreements"[191] have generally been of two types. The first is to fash-

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tion context. *See, e.g.*, Rafe v. Hindin, 29 App. Div. 2d 481, 288 N.Y.S. 2d 662, 663-64 (1968)(restriction which did not provide that consent would not be unreasonably withheld was invalid restraint on alienation). Of course, even where such a restriction was validly entered into, a court might refuse to enforce it if consent is wrongfully withheld, *e.g.*, as a means of forcing a sacrifice sale.

[188] *See* New MBCA, *supra* note 1, § 6.,27 (a), (b). This is likewise necessary under the Mississippi Uniform Commercial Code. MISS. CODE ANN. § 75-8-204 (1972).

[189] *See* Old MBCA, *supra* note 1, § 65.

[190] *See, e.g.*, E.K. Buck Retail Stores v. Harkert, 157 Neb. 867, 881, 62 N.W. 2d 288, 302 (1954)(upholding agreement by majority and minority stockholders to vote their shares in such a way as to maintain equal board representation).

[191] It should be emphasized that this discussion deals only with agreements respecting matters as to which shareholders are competent to act, primarily the election of directors. Agreements by shareholders encroaching upon board authority are dealt with at

ion an appropriate enforcement mechanism.[192] An irrevocable proxy to an arbitrator or non-defaulting shareholder would seem an obvious answer. In those states without specific statutory authorization for irrevocable proxies, however, one would have to argue that it was rendered irrevocable as a proxy coupled with an interest.[193] This was not clearcut by any means. Moreover, it bore upon the second problem, *i.e.*, whether a pooling agreement might be invalidated as constituting a voting trust that did not comply with statutory requirements.[194] Clearly, statutory definition of the acceptable parameters of such agreements is the preferable approach.

The New MBCA responds to both concerns. Section 7.31 grants broad authority for shareholders to enter into agreements defining "the manner in which they will vote their shares."[195] The statute makes such agreements specifically enforceable, and

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infra notes 199-201 and accompanying text.

[192] The classic case was Ringling v. Ringling Bros. Barnam & Bailey Combined Shows, Inc., 29 Del. 318, 49 A.2d 603 (Ch. 1946), *modified*, 29 Del. 610, 53 A.2d 441 (1947), in which the parties agreed that in the event of a disagreement, the matter would be submitted to an arbitrator whose decision would be binding. Since the agreement did not provide a right for the arbitrator to actually vote a defaulting party's shares, however, the Delaware Supreme Court reversed the Chancellor's decision to imply a proxy. Thus, the Supreme Court remedied the breach by refusing to count the defaulters' shares in the election of directors. Unfortunately for the plaintiff, without the defaulter's votes the plaintiff was outvoted by a competing shareholder, who thereby gained control of the corporation. *Ringling*, 29 Del. at 614, 53 A.2d at 244. *See* Note, *Specific Enforcement of Shareholder Voting Agreements*, 15 U. Chi. L. Rev. 738 (1947)(specific enforcement of unobjectionable voting agreements desirable as matter of public policy).

[193] Prior Mississippi law had no express provision for irrevocable proxies. *See* Old MBCA, *supra* note 1, § 63.

[194] Again the classic case came from Delaware. In Abercrombie v. Davies, 36 Del. 371, 130 A. 2d 338 (1957), the court struck down an "Agent's Agreement" under which shareholders deposited their shares with agents who were granted irrevocable proxies to vote the shares for a period of ten years. *Id.* at 376, 130 A. 2d at 344. The court held that this was a secret voting trust that violated the requirements of the voting trust statute. *Id.* In distinguishing this arrangement from the valid pooling agreement in *Ringling*, the court emphasized *inter alia* the absence of irrevocable proxies in *Ringling*. *Id.* at 377-78, 130 A. 2d at 345-46. *Abercrombie* was subsequently overruled in substance by the Delaware Legislature, *see* Del. Code Ann. tit. 8, § 218(c), (e)(1968), and the Delaware Supreme Court has apparently retreated somewhat from its rigorous application. *See* Oceanic Exploration Co. v. Grynberg, 428 A.2d 1, 6-7 (Del. 1981)(voting trust provisions which were part of broad agreement of corporate reorganization were not subject to voting trust statute restrictions).

[195] *See* New MBCA, *supra* note 1, § 7.31(a).

provides that proxies granted by parties to such agreements are irrevocable.[196] Finally, the act specifically excludes such agreements from the voting trust statute, section 7.30.[197]

On the other hand, it must be emphasized that these sections do not govern shareholder control agreements that affect the discretion of the board of directors. Under the 1988 amendments, the New MBCA now conforms to the RMA and allows a corporation with fifty or fewer shareholders to dispense entirely with the board of directors and be governed by its shareholders in the fashion of partnerships.[198] Absent this right of direct shareholder management, planners must draft cautiously any provisions that seek to control the board's powers of management lest they run afoul of common-law resistance to such attempts.[199] While courts have tended recently to view such agreements more favorably,[200] even unanimous shareholder agreement cannot guarantee that such agreements are immune to attack.[201] Unfortunately, the range of judicially permissible options remains murky at best.

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[196] *Id.* §§ 7.22(d)(5), 7.31(b).

[197] *Id.* § 7.31(a). The voting trust provisions do not materially differ from prior law.

[198] MISS. CODE ANN. § 79-4-8.01(c) (Supp. 1988); *see* REVISED MODEL BUSINESS CORP. ACT § 8.01(c) (1984). This issue is also discussed in *Part One*, *supra* note 3, at 183-84 n.68. The legal impediment to this originally was section 194 of the Mississippi Constitution, which could have been interpreted as requiring a board of directors for all corporations. As previously noted, section 194 has since been repealed. *See supra* note 36.

Of course, the 50 shareholder limit is subject to the criticism of arbitrariness, but since it appears in the RMA it has the merit of uniformity.

[199] *See, e.g.* Long Park, Inc. v. Trenton-New Brunswick Theatres Co., 297 N.Y. 174, 175-76, 77 N.E.2d 633, 634-35 (1948)(agreement delegating management powers to majority shareholder for 19 years "completely sterilized" board and was therefore against public policy); McQuade v. Stoneham, 263 N.Y. 323, 325-26, 189 N.E. 234, 236-37 (1934)(agreement providing *inter alia* that shareholders would occupy certain offices and be paid fixed salaries was invalid attempt to control board where non-party minority interest existed). *But see* Clark v. Dodge, 269 N.Y. 410, 412, 199 N.E. 641, 643 (1936)(slight invasions of powers of directorate by shareholders is permissible where all shareholders are parties and creditors are not threatened).

[200] The leading case is probably Galler v. Galler, 32 Ill. 2d 16, 203 N.E.2d 577 (1964), which upheld an agreement between two shareholders owning 208 of 220 shares that required the payment of annual dividends and fixed salaries to their wives for five years after the death of a signatory shareholder. *Id.* at 27, 203 N.E. 2d at 587. The court formulated the applicable test as no public injury, no complaining minority interest, and no prejudice to creditors. *Id.* at 25, 203 N.E. 2d at 585. Again, however, even *Galler* cannot be interpreted as meaning that "anything goes" if all shareholders agree. *See e.g.*, Somers v. AAA Temporary Services, Inc., 5 Ill. App.3d 931, 932-33, 284 N.E.2d 462, 464-65 (1972)(voiding bylaw amendment passed by shareholders rather than directors; held that *Galler* did not permit direct contravention of statute).

From a policy perspective it would seem that shareholders of a close corporation, acting unanimously, should have the same freedom to order and manage their affairs by agreement as partners of general partnerships have, without regard to the artificial distinctions of shareholders and directors.[202] This flexibility can now be achieved in Mississippi under the amended New MBCA;[203] however simply providing for direct shareholder management for a qualified corporation does not obviate the need for carefully structured control agreements analogous to those utilized in partnerships. As with partners such matters are appropriately governed contractually, not through a statutory model which is simply unrealistic in most close corporations.

D. Dissention and Deadlock

It is in the area of remedies for deadlock that the New MBCA is perhaps most deficient. As previously discussed, the act now allows a court to appoint a custodian to manage the affairs of a solvent corporation, which is certainly an improvement over prior law.[204] However, the grounds for judicial dissolution under section 14.30 are basically the same as under prior law, requiring a showing of irreparable harm in the event of director deadlock, shareholder deadlock preventing election of directors for two years, "illegal, oppressive or fraudulent" actions of directors or majority shareholders, or misapplication or waste of assets.[205] Thus the new act does not include more liberal provisions of some modern statutes allowing, *e.g.*, dissolution where the business cannot function to the benefit of shareholders generally or pursuant to any provision in the articles.[206] Given the traditional disinclination of courts to order dissolution and the stringency of such standards as irreparable injury, fraud, oppression, and waste, the statute is arguably an inadequate response to the plight of the minority shareholder who may find himself locked into an inviable investment without the "Wall Street Option" of public corporation shareholders to sell in a waiting market.

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[201] The *Long Park* decision is a frequently cited example. *See supra* note 199.

[202] *See* Bradley, *Toward A More Perfect Close Corporation - The Need for More and Improved Legislation*, 54 Geo. L. J. 1145, 1183 (1966)(close corporation should provide for validity of unanimous agreements affecting management on control of corporation).

[203] *See supra* note 198 and accompanying text.

[204] *See supra* notes 148-151 and accompanying text.

[205] *See* New MBCA, *supra* note 1, § 14.30(2).

The problem of illiquidity of the close corporation investment, particularly a minority interest, is probably the most vexing one still facing legislators and close corporation planners. The "liquidation right"[207] of partners in a general partnership, even one constituted for a term,[208] simply is not part of the corporate model. While the appropriate statutory response has been much debated, I would favor the approach of authorizing provisions in the articles of smaller corporations (to be consistent, those with fifty or fewer shareholders) granting any shareholder, or holders of a specified number or percentage of shares, the option to cause dissolution at will or upon the occurrence of a specified event or contingency.[209] While this may be criticized as giving individual shareholders too much leverage over the majority, it simply approximates the partnership model and, in any event, would be subject to arms-length negotiation at the time of incorporation. Such a statute should require unanimous consent of shareholders to any amendment of the articles to provide the right, and for legending share certificates to protect innocent purchasers. So long as all parties approach the issue with eyes open, this seems a preferable alternative to the risks run by minority shareholders without such a cash-out option.[210]

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[206] *E.g.*, S.C. CODE § 33-21-150 (1976).

[207] This was the term coined by Professor Bromberg. Bromberg, *Partnership Dissolution — Causes, Consequences, and Cures*, 43 TEX. L. REV. 631, 647 (1965).

[208] *See* MISS. CODE ANN. § 79-12-75 (Supp. 1987)(Mississippi Uniform Partnership Act provision on withdrawal of partners).

[209] *See, e.g.*, DEL CODE ANN. tit. 8, § 355 (a)(1968)(allows stockholders option to dissolve corporation at will or upon specified event or contingency).

[210] Of course, the minority can also be protected in the event of dissent by buy-out agreements, but these presuppose both the willingness of majority shareholders to assume this obligation and the financial ability to follow through. On the other hand, it would be disingenuous to think that "at-will dissolution" will not in some instances be

V. MISCELLANEOUS

A. Foreign Corporations

The New MBCA provisions on foreign corporations[211] do not merit extensive discussion. There is, however, one important change in the area of qualification to do business. As is well known, the "door closing" provision of the Old MBCA,[212] which denied access to state courts to foreign corporations that transacted business in Mississippi without a certificate of authority, was narrowly construed by the Mississippi Supreme Court to preclude a corporation from suing on any cause of action that arose prior to qualification. Subsequent qualification would not retroactively cure the defect.[213] This punitive rule is reversed by the New MBCA, which expressly provides that a foreign corporation transacting business without a certificate of authority cannot bring an action in state court "*until* it obtains a certificate of authority," and allows a court to stay any proceeding un-

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used as a leverage device in negotiations between dissenting factions.

It should be noted that the suggested approach is by no means the most radical one that has been advanced. It does not, for example, protect the shareholder who does not bargain for and obtain the right to dissolve at will. In an important article, Professors Hetherington and Dooley advocated that this gap be closed statutorily by granting any minority shareholder in a close corporation the right to force the corporation to purchase all his shares at their fair value, so long as this would not render the corporation insolvent. This right would also be nonwaivable after two years from incorporation. Hetherington & Dooley, *Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 50-52 (1977). While provocative, I do not view this as a workable proposal at this time. For other criticisms, see Hillman, *The Dissatisfied Participant in the Solvent Business Venture: A Consideration of the Relative Permanence of Partnerships and Close Corporations*, 67 MINN. L. REV. 1, 69-75 (1982) (questioning assumptions upon which advocation of at will dissolution by minority shareholders is based).

[211] *See* New MBCA, *supra* note 1, Chapter 15.

[212] *See* Old MBCA, *supra* note 1, § 247.

[213] Parker v. Lin-Co. Producing Co., 197 So. 2d 228, 230 (Miss. 1967). This, of course, was contrary to the general rule in other states. *See* Dunn-Cooper, *An Analysis of Mississippi's Treatment of Foreign Corporations*, 55 MISS. L. J. 259, 261-62 (1985)(examination of Mississippi's rule).

Ironically, the Mississippi Supreme Court reached the opposite conclusion as to foreign limited partnerships, holding that qualification applied retroactively. MISS CAL 204, Ltd. v. Upchurch, 465 So.2d 326 330 (Miss. 1985)(construing MISS. CODE ANN. § 79-13-213(1)(Supp. 1987), *repealed*, 1987 Miss. Laws ch. 448, § 1105).

til the foreign corporation obtains the certificate.[214]

B. Conflicts of Interest

While director conflicts of interest were discussed extensively in Part One of this Article,[215] one aspect of the New MBCA as enacted deserves additional comment. I previously advocated the adoption of a statute modeled after Illinois law and the Exposure Draft of the RMA explicitly providing that director or shareholder ratification of a conflict of interest transaction did not validate it for all purposes, but simply shifted the burden of proof on the ultimate issue of fairness to those attacking the transaction. The Legislature, however, adopted the approach of the RMA, with one modification: shareholder ratification requires the vote of two-thirds of eligible shares, rather than a majority.[216]

I believe that the Legislature intended to enact only a savings statute that defines the burden of proof of fairness, but does not otherwise validate an unfair transaction. However, this provision — while apparently adopted with the salutary objective of making ratification logistically more difficult—may ultimately yield an undesirable result. By increasing the requisite percentage for ratification, the statute may be susceptible to a construction that the more onerous vote requirement should thereafter shield the transaction from judicial review. For reasons I have already discussed in Part One at length, I do not believe that this is sound policy. Thus I would urge the Legislature to correct this ambiguity in the New MBCA by express provision that it is intended only to shift the burden of proof, not to imbue a conflict of interest transaction with absolute validity.[217]

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[214] *See* New MBCA, *supra* note 1, § 15.02 (a), (c)(emphasis added).

[215] *See Part One*, *supra* note 3, at 202-11 (discussion of duty of loyalty).

[216] *See* New MBCA, *supra* note 1, § 8.31 (d).

[217] In fairness I should note that this is clearly not the position now adopted by the ABA Committee on Corporate Laws. The most recent amendment to the RMA proposed by the Committee is a new Subchapter F governing directors' conflict of interest transactions. Among other things the proposed amendment would absolutely prohibit any judicial attack on a transaction that was approved by either the board or shareholders according to statutorily prescribed procedures. *See* Committee on Corporate Laws, *Changes in the Model Business Corporation Act — Amendments Pertaining to Director's Conflicting Interest Transactions*, 43 BUS. LAW. 691 (1988).

C. Cumulative Voting

Part One of this article advocated the elimination of mandatory cumulative voting.[218] Thus it is satisfying to note that, with the repeal of section 194 of the Constitution,[219] the Legislature has now amended the new Act to make cumulative voting permissive, although the right to cumulate applies unless eliminated by the articles.[220]

VI. CONCLUSION

The 1987 Mississippi Business Corporation Act undoubtedly represents a substantial improvement over its predecessor. Nonetheless, as both Parts of this Article have attempted to illustrate, there is much room for further refinement of the statute, and the experience of the bench and bar will undoubtedly expose even more areas which need legislative attention. One hopes that the Mississippi Legislature's history of "benign neglect" of the 1962 MBCA will not be indicative of its attitude towards our new Act; the 1988 amendments are an encouraging sign to the contrary.[221] In any event, the sweeping changes that it has already effected sound a call to immediate attention by Mississippi corporate practitioners.

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[218] *Part One*, *supre* note 3, at 228-31.

[219] *See supra* note 36.

[220] MISS. CODE ANN. § 79-4-7.28(b) (Supp. 1988). A conforming amendment was also made to section 8.08, dealing with director removal.

The 1988 amendments also now permit, *inter alia*, directors to fill vacancies in the board, unles prohibited by the articles. MISS. CODE ANN. § 79-4-8.10 (a) (2) (Supp. 1988).

[221] *See generally* 1988 Miss. Laws Chs. 368-69.

BUYER'S DAMAGES FOR BREACH IN REGARD TO ACCEPTED GOODS

*Roy Ryden Anderson**

I. Introduction

A. General Overview

The action a buyer takes in response to a breach by the seller will determine the damage remedies available to him under the Uniform Commercial Code. The buyer can choose to reject the goods as provided in section 2-602[1] or revoke his acceptance of them under section 2-608[2] and, in either case, recover damages as provided in section 2-711(1).[3] Alternatively,

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[1] U.C.C. § 2-602 (1)(1978). The statute states that "[r]ejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller." *Id.*

[2] *Id.* § 2-608 (1978). The section provides:

> (1) The buyer may revoke his acceptance of a lot or commercial unit whose non-conformity substantially impairs its value to him if he has accepted it
>
> (a) on the reasonable assumption that its non-conformity would be cured and it has not been seasonably cured; or
>
> (b) without discovery of such non-conformity if his acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller's assurances.
>
> (2) Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. It is not effective until the buyer notifies the seller of it.
>
> (3) A buyer who so revokes has the same rights and duties with regard to the goods involved as if he had rejected them.

Id.

[3] *Id.* § 2-711(1). This section provides:

> (1) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (section 2-612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid
>
> (a) "cover" and have damages under the next section as to all the goods

the buyer might choose to accept the goods or fail to meet the requirements for revoking acceptance of them. The purpose of this article is to analyze the Code provisions and accompanying case law applicable to measuring buyers' damages in situations in which the sellers' breach is such that the buyer either may not or chooses not to return the affected goods to the seller. Section 2-714 provides the exclusive damage remedy for a buyer who has accepted goods without effectively revoking his acceptance.[4] The proposition that section 2-714 is the sole remedy for accepted goods is apparent from the text of the statute,[5] as well as from Official Comments 1 and 3 thereto,[6] and has been widely recognized by the courts.[7]

> affected whether or not they have been identified to the contract; or
> b) recover damages for non-delivery as provided in this Article (section 2-713).

Id.

[4] *See* J. White and R. Summers, Handbook of the Law Under the Uniform Commercial Code 375 (2d ed. 1981)("[O]nly buyers who have accepted and neither rightfully rejected nor effectively revoked can use 2-714. Thus, in our view, sections 2-713 [market formula] and 2-712 [cover formula] on the one hand and 2-714 on the other are mutually exclusive.")

[5] Section 2-714 of the Uniform Commercial Code provides:

> (1) Where the buyer has accepted goods and given notification (subsection (3) of section 2-607) he may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any manner which is reasonable.
> (2) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.
> (3) In a proper case any incidental and consequential damages under the next section may also be recovered.

Id.

[6] *See* U.C.C. § 2-711 comments 1 and 3 (1978)(implying that § 2-714 is sole remedy for accepted goods). *See also* Rutherford v. Darwin, 622 P.2d 245, 248 (N.M. Ct. App. 1980)(even though not binding on court, official comment is persuasive of Code section meaning).

[7] *See* Wolfes v. Terrell, 173 Ga. App. 835, 328 S.E.2d 569, 571 (1985)(section 2-714 applies only where buyer claims breach of contract regarding accepted goods and therefore is not proper measure of damages for action arising from rejection, revocation of acceptance or rescission of purchase contract); Solomon Refrigeration, Inc. v. Osburn, 148 Ga. App. 772, 252 S.E.2d 686, 690 (1979)(section 2-714 applies only when time for revocation has passed); Galigher Trucks, Inc. v. McKenzie, 553 S.W.2d 294, 295 (Ky.Ct. App. 1977)(where buyer has not revoked acceptance or rejected goods and goods are not as warranted, damages awarded pursuant to § 2-714(2)); General Motors Acceptance

Thus, it is requisite to an action for damages under section 2-714 that the buyer have accepted the goods.[8] Acceptance occurs when the buyer, after having had a reasonable opportunity to inspect the goods, either notifies the seller that he will keep the goods or simply remains silent as to any intention to reject them.[9] A buyer's delay in deciding whether to accept or reject the goods may constitute an acceptance, thereby limiting his remedy to that afforded him by section 2-714.[10] Acceptance can occur at any time if the buyer acts in consistently with the seller's ownership of the goods.[11] But the buyer may be able to

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Corp. v. Anaya, 703 P.2d 169, 171 (N.M. 1985)(buyer need not elect between distinct claims of revocation of acceptance and breach of warranty at trial, but once jury finds that buyer has successfully proven all elements essential to establish rightful revocation, trial court may properly deem breach of warranty theory extinguished); Agar v. Kysar, 628 P.2d 1350, 1352-53, (Wyo. 1981)(complaint alleging breach of warranty cannot constitute notice of revocation of acceptance because implication under Code is that buyer intends to keep goods). *But see* AFA Corp. V. Phoenix Closures, Inc., 501 F. Supp. 224, 230 (N.D. Ill. 1980)(awarding breach of warranty damages under § 2-714(2) and holding buyer entitled to revoke acceptance); Warren v. Guttanit, Inc., 317 S.E.2d 5, 11-13 (N.C.Ct. App. 1984)(allowing damages under both § 2-711 and § 2-714 despite finding that buyer had revoked acceptance).

[8] *See, e.g.*, In re Giles World Marketing, Inc., 29 Bankr. 523 (Bankr. D. Mass. 1983)(since seller never tendered goods to buyer, buyer had no opportunity to accept goods; therefore, buyer has no right to remedies under U.C.C. § 2-714).

[9] U.C.C. § 2-606 (1978). The Code provides:

> (1) Acceptance of goods occurs when the buyer
>
> (a) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he will take or retain them in spite of their non-conformity; or
>
> (b) fails to make an effective rejection (subsection (1) of section 2-602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or
>
> (c) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.
>
> (2) Acceptance of a part of any commercial unit is acceptance of that entire unit.

Id.

[10] Intervale Steel Corp. v. Borg & Beck Div., Borg-Warner Corp., 578 F. Supp. 1081, 1085-86 (E.D. Mich. 1984)(when rejection not made within reasonable time under § 2-602, buyer is deemed to have accepted goods under § 2-606 making § 2-714 the appropriate remedy); Kee v. Campbell, 8 Kan. App. 2d 561, 661 P.2d 831, 832 (1983)(buyer limited to recovery of damages for breach of warranty under § 2-714 where neither rejection nor revocation of acceptance was timely).

[11] U.C.C. § 2-606(1)(c)(1978).

revoke his acceptance if he can meet the requirements of section 2-608. However, revocation of acceptance may prove to be difficult. Since section 2-608 requires that a breach constitute a substantial impairment of the value of goods, not every breach entitles a buyer to revoke his acceptance.[12]

Section 2-714 contains three subsections.[13] Subsection (1) allows the buyer to recover damages for "any non-conformity of tender" as to goods the buyer has accepted. Damages are to be "determined in any manner which is reasonable."[14]

Where the seller's breach is one of warranty, subsection (2) provides a specific formula for calculating damages for accepted goods. The buyer is entitled to recover "the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted."[15] This value differential formula is to apply "unless special circumstances show proximate damages of a different amount." [16]

Subsection (3) merely authorizes the recovery of incidental and consequential damages "in a proper case." A "proper case" is one that meets the requirements set forth in section 2-715.[17]

In keeping with general principles of contract law and with the specific mandate of the Code, section 2-714 damages are intended to place the aggrieved buyer in as good a position as he would have occupied had the seller performed as promised.[18]

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[12] Fargo Mach. & Tool Co. v. Kearney & Trecker Corp., 428 F. Supp. 364, 377-78 (E.D. Mich. 1977). Section 2-608 requires that the buyer notify the seller of revocation, that the revocation must occur within a reasonable time after the buyer discovers the grounds, that the non-conformity has substantially impaired the value of the goods and that the revocation occurs before any substantial changes in the goods other than by their own defects. U.C.C. § 2-608 (1978).

[13] U.C.C. § 2-714 (1978).

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] U.C.C. § 2-714 (1978) comment 4.

[18] *See* U.C.C. § 1-106 (1). This section provides:

> The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law.

Id.

Thus, regardless of the subsection used for the calculation, the recovery of the buyer should reflect the benefit of the bargain made and the lost expectation caused by the breach.[19]

While section 2-714 will allow a buyer to recover the economic benefit of a good bargain, it will not help a buyer who simply made a bad deal.[20] For example, assume that the buyer purchased goods that would have had a fair market value of $10,000 had they been as warranted. The goods are defective, but the buyer chooses to accept them and pass them on to his customers at a discount. The resale value of the goods was only $9,000. Section 2-714(2) would allow the buyer to recover $1,000 based on the difference in the value of the goods accepted ($9,000) and the value they would have had if they had been as warranted ($10,000). In this way, the buyer would be allowed the benefit of the bargain he made.

On the other hand, assume the buyer made (as it turns out) a bad deal by agreeing to purchase the goods for a price of $10,000 when their value at the time of delivery as warranted would be only $8,000. The goods are defective, so that their value at the time of delivery is actually only $7,500. If the buyer nevertheless accepts the goods, his damages under section 2-714 will be only $500, the difference between their value as warranted ($8,000) and their value as received ($7,500). Having accepted the goods, the buyer will be required to pay the full contract price of $10,000[21] and will only receive $8,000 in value ($7,500 in goods and $500 in damages). Such was the (bad) bargain the buyer made, and section 2-714 reflects the bargain for good or bad. In a case like our hypothetical, where the buyer has made an unfortunate deal, his best recourse is to reject the goods rather than accept them. The buyer will avoid liability to the breaching seller for his contract price and can go into the market and purchase the goods for their going market price.[22]

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[19] Reynolds Metal Co. v. Westinghouse Elec. Corp., 758 F.2d 1073, 1079 (5th Cir. 1985). The *Reynolds* court, citing § 2-714, stated that both common law and the Uniform Commercial Code generally authorize damages for breach calculated as the amount of the expectancy interest of the wronged party. *Id.* The victim of the breach is entitled to be placed in the same position he would have occupied had the breach not occurred. *Id.* The court found the three principal elements to such damages to be

> (1) general difference in value losses - the difference in value to the wronged party of the performance on goods tendered and the performance of goods tendered and the performance of goods as promised under the contract; (2) incidental losses - costs incurred in a reasonable effort, whether successful or not, to avoid losses caused by the breach; and (3) consequential losses -items such as lost profits or injuries to person or property foreseeable caused by the breach.

Id. See also Bunch v. Signal Oil & Gas Co., 505 P.2d 41, 43 (Colo. Ct. App. 1972)(upon proving breach of contract, plaintiff entitled to be placed in same position he would have occupied had contract not been breached); Acme Pump Co., Inc. v. National Cash Register Co., 33 Conn. Supp. 69, 337 A.2d 672, 677, (Conn. 1974)(loss directly and naturally resulting from breach is proper measure of damages under § 2-714 and damages awarded should essentially place plaintiff in same position as plaintiff would have been in had defendant fully performed the contract); Colonial Discount Corp. v. Berkhardt, 435 N.E.2d 65, 66 (Ind. Ct. App. 1982)(under § 2-714, non-breaching party is not entitled to be placed in better position than he would have been in had contract been fully performed); S.C. Gray, Inc. v. Ford Motor Co., 92 Mich. App. 789, 286 N.W. 2d 34, 43 (Mich. Ct. App. 1979)(section 2-714(2) damages for breach of contract intended to place injured party in as good a position as he would have been in had performance been rendered).

[20] *See* J. WHITE AND R. SUMMERS, *supra* note 4, at 376 (important element not recoverable under § 2-714 is cost of bad bargain).

The "special circumstances" language in subsection (2) has been interpreted in a variety of ways by the courts.[23] In essence, "special circumstances" exist whenever the situation does not lend itself to a value differential calculation or when that calculation fails to place the buyer in the position he would have occupied had the contract been properly performed by the seller. The net effect is that "special circumstances" take the case out of subsection (2) and into the general rule of subsection (1) so that damages are "determined in any manner which is reasonable."[24]

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[21] *See* U.C.C. § 2-607(1)(1978)(buyer must pay contract price for any goods accepted).

[22] *See* B. Clark & C. Smith, The Law of Product Warranties § 7.05[1] (1984)(escape from bad bargain available if buyer rejects goods or revokes acceptance and covers on open market), In a hypothetical White and Summers use fair market value and resale price respectively as the value of the tomatoes as warranted and as accepted, one way of measuring the value-differential under § 2-714(2). J. White and R. Summers, *supra* note 4, at 376-77. *See infra* notes 31-177 and accompanying text for further discussion.

[23] *See* J. White and R. Summers, *supra* note 4, at 383 (most courts use objective criteria to determine market value; expansive definition of "special circumstances" would provoke subjective outcome).

[24] U.C.C. § 2-714 (1)(1978). *See* Lackawanna Leather Co. v. Martin & Stewart, Ltd., 730 F.2d 1197, 1203 (8th Cir. 1984)(while typical measure of damages for breach of warranty cases is value-differential formula, § 2-714 (1) provides that such damages are to be determined "in any manner which is reasonable").

Comment 2 to section 2-714 makes clear that the "non-conformity" referred to in subsection (1) includes not only breaches of warranty, but also any other failure of the seller to perform according to his contractual obligations.[25] Virtually all of the reported cases to date under section 2-714, however, have involved a breach of warranty.[26]

The only distinction between section 2-714's treatment of breaches of warranty and other non-conforming tenders is the time at which the damages are to be fixed. Damages for breach of warranty are fixed at the time and place of acceptance.[27] Damages for other non-conforming tenders are fixed at the time and place of tender.[28] Frequently the time and place of both tender and acceptance will be the same; *i.e.*, the buyer will signify acceptance upon tender.[29]

It has been suggested that section 2-714 is best understood when considered in light of four basic tenets:

> (1) The court awarding damages for a breach of warranty should endeavor to place the aggrieved party in the position in which performance would have placed him; no more and no less.
> (2) The court should encourage the parties to minimize the damage flowing from a breach of warranty.
> (3) The court, where consistent with public and statutory policies, should respect the intentions of the parties.

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[25] U.C.C. § 2-714 comment 2 (1978).

[26] *See* Ford Motor Credit Co. v. Harper, 671 F.2d 1117, 1121-22 (8th Cir. 1982)(breach of warranty and nonconformity are not entirely congruent concepts where former is subset of latter); Bendix Home Systems, Inc. v. Jessop, 644 P.2d 843, 845,(Alaska 1982)(goods may be "non-conforming for variety of reasons, one of which is failure to meet implied warranty of merchantability"); Michiana Mack, Inc., v. Allendale Rural Fire Protection Dist., 428 N.E.2d 1367, 1370 (Ind. Ct. App. 1981)("nonconformity" is term of art used to describe both breach in goods and in conduct).

[27] U.C.C. § 2-714 (2)(1978). However, comment 3 states an exception to the general rule: "[i]f, however, the non-conformity is such as would justify revocation of acceptance, the time and place of acceptance under this section is determined as of the buyer's decision not to revoke." *Id.* comment 3.

[28] *Id. See also* W. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES, § 2-714:02, 375 (1982)(measure of damages for breach of warranty is established at time and place of acceptance; for other kinds of breaches in regard to accepted goods, measure of damages is fixed at time and place of tender).

[29] U.C.C. § 2-714 comment 3 (1978).

(4) The court should be guided not by semantics but by common sense, commercial practicality and Code policies.[30]

These tenets represent good practice no matter the damage remedy involved.

B. The Notice Requirement

Once the buyer has accepted the goods, it is a prerequisite to an action based on section 2-714 that the buyer provide the seller with seasonable notice of the breach. Section 2-607(3)(a) provides that "where a tender has been accepted . . . the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from any remedy . . . ."[31] The notice requirement is not a stringent one and "need only be such as informs the seller that the transaction is claimed to involve a breach, and thus open the way for normal settlement through negotiation."[32] Consumer buyers are given greater latitude than are merchants,[33] but neither is required to give notice of breach in writing.[34] An occasional case has held that notice of breach is not required where, as in cases of late delivery of the goods, the seller is already aware of the breach.[35]

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[30] Special Project, *Article Two Warranties in Commercial Transactions*, 64 CORNELL L. REV. 30, 104-05 (1978). The reader may wish to review the following sections of the Uniform Commercial Code insofar as they are interrelated with § 2-714:

§ 1-102.Purposes; Rules of Construction; Variation by Agreement
§ 1-106.Remedies to be Liberally Administered;
§ 1-203.Obligation of Good Faith;
§ 2-209.Modification, Rescission and Waiver;
§ 2-717.[Buyer's] Deduction of Damages From the Price.

This listing is intended only to point out some of the more important Code provisions that may bear on the question of damages for accepted goods.

[31] U.C.C. § 2-607 (3)(a)(1978).

[32] *Id.* § 2-607 comment 4. This comment states in full:

> The time of notification is to be determined by applying commercial standards to a merchant buyer. 'A reasonable time' for notification from a retail consumer is to be judged by different standards so that in his case it will be extended, for the rule of requiring notification is designed to defeat commercial bad faith, not to deprive a good faith consumer of his remedy.
>
> The content of the notification need merely be sufficient to let the seller know that the transaction is still troublesome and must be watched. There is no reason to require that the notification which saves the buyer's rights under this section must include a clear statement of all the objections that will be relied on by the buyer, as under the section covering statements of defects upon rejection (Section 2-605). Nor is there reason for requiring the notification to be a claim for damages or of any threatened litigation or other resort to a remedy.

> The notification which saves the buyer's rights under this Article need only be such as informs the seller that the transaction is claimed to involve a breach, and thus opens the way for normal settlement through negotiation.

Id.

[33] U.C.C. § 2-607 comment 4.

[34] *See* Reynolds Metal Co. v. Westinghouse Elec. Corp., 758 F.2d 1073, 1078 (5th Cir. 1985)(question of adequacy of § 2-607 notice is one of liberal construction and depends on reasonableness of efforts of wronged party to communicate dissatisfaction with the tendered performance considering all circumstances); Smart Chevrolet Co. v. Davis, 558 S.W.2d 147, 148 (Ark. 1977)(U.C.C. does not require written notice to assert claim for breach of warranty); United States Fidelity & Guar. Co. v. North Am. Steel Corp. 335 So. 2d 18, 22 (Fla. Dist. Ct. App. 1976)(with respect to notifying seller of any breach within reasonable time, any time which is not manifestly unreasonable may be fixed by agreement per § 1-204).

[35] *See, e.g.*, Jay V. Zimmerman Co. v. General Mills, Inc., 327 F. Supp. 1198, 1204 (E.D. Mo. 1971) where the court held:

> In the present, as in any case involving late delivery, both the seller and the buyer are necessarily fully aware *prior* to tender that the seller's contract obligation to timely deliver has not been complied with. It would be an unreasonable, if not absurd, construction of the statute to require a renewed notice of breach *after* acceptance of the goods under the facts here involved. A party has notice of a fact when he has actual knowledge of it. [§ 1-201(25)]. The purpose of a notice in the context of this section is to *inform* the seller of matters which would not normally come to the buyer's attention until *after* the goods came into his possession. The legislative intent was to make provision with respect to the effect of acceptance of allegedly defective or inferior goods or those not meeting warranted standards of quality. In that situation it is reasonable to require the buyer to inform the seller of the existence of a possible factual dispute relating to matters of which the buyer presumably was not aware prior to his acceptance of a tender of the goods. (emphasis in original)

Id.

Although there is a certain logic to the court's reasoning in *Jay V. Zimmerman Co.*, it is flawed. While the seller may be fully aware that his delivery is late, he may not be aware that the buyer views the delay as a breach of contract. By notifying the seller of this fact, the buyer "opens the way for normal settlement through negotiation." U.C.C. § 2-607 (1978) comment H. The better rule, reflected in cases decided both prior to the adoption of the Code and under it, has been to require the buyer to notify the seller that he considers the contract in breach regardless of whether the seller is aware of his failure to perform in accordance with the contract. *See* Columbia Axle Co. v. American Auto. Ins. Co., 63 F.2d 206, 208 (6th Cir. 1933)(burden on buyer to show by substantial evidence that seller waived notice requirement). In American Mfg. Co. v. United States Shipping Bd. Emergency Fleet Corp., Judge Learned Hand made the following

However, requiring notice in every case is the better rule, since it establishes a "bright line" test to guide merchants' behavior and provides a mechanism for closing the door to potential litigation.

II. CALCULATION OF DAMAGES

A. *The General Rule - Section 2-714(1)*

Section 2-714(1) states the general rule for the buyer's recovery of damages for breach in regard to accepted goods. The rule is that the buyer "may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any manner which is reasonable."[36] The Official Comment to section 2-714 explains that: "The 'non-conformity' referred to in subsection (1) includes not only breaches of warranties but also any failure of the seller to perform according to his obligations under the contract."[37] Although subsection (2) states a specific rule for measuring damages for breach of warranty, an exception is made if "special circumstances show proximate damages of a different amount."[38] The effect of the "special circumstances" exception is to take the damage calculation out of subsection (2) and to place it in subsection (1) so that damages are "determined in any manner which is reasonable."[39]

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observation:

> The plaintiff replies that the buyer is not required to give notice of what the seller already knows, but this confuses two quite different things. The 'notice of the breach' required is not of the facts, which the seller presumably knows quite as well as, if not better than, the buyer, but of buyer's claim that they constitute a breach. The purpose of the notice is to advise the seller that he must meet a claim for damages, as to which, rightly or wrongly, the law requires that he shall have early warning.

American Mfg. Co. v. United States Shipping Bd. Emergency Fleet Corp., 7 F.2d 505, 566 (2d Cir. 1925). *See also* Standard Alliance Indus., Inc. v. Black Clawson Co., 587 F.2d 813, 825 (6th Cir. 1978), (quoting Judge Learned Hand regarding § 49 of the Uniform Sales Act, predecessor of § 2-607), *cert. denied*, 441 U.S. 923 (1979).

[36] U.C.C § 2-714 (1)(1978).

[37] *Id.* at comment 2.

[38] *Id.* § 2-714 (2).

[39] *Id.* § 2-714 (1). *See* Ralston Purina Co. v. Hartford Accident & Indem. Co., 540 F.2d 915, 920 (8th Cir., 1976)(section 2-714(1) permits buyers to recover damages or any loss resulting in ordinary course of events from seller's breach as determined in any rea-

Subsection (1) has been applied so as to award damages to a buyer who failed to allege or offer proof on the issue of the value of the goods accepted.[40] In *Fargo Machine and Tool Co. v. Kearney* this failure made proof of damages impossible under subsection (2).[41] The court was able to muster enough evidence from the record to award a modicum of damages and reasoned that subsection (1) allowed it to compute the buyer's loss " 'in any manner which is reasonable'."[42] Although the language in subsection (1) is much broader than that of subsection (2), both provisions seek to provide the buyer the benefit of his bargain by approximating in monetary terms the lost expectation caused by the seller's breach.[43] The significant majority of cases decided under section 2-714 involve breaches of warranty, and damages, therefore, are calculated under subsection (2).[44] Of the smattering of "non-conformity of tender" cases decided under subsection (1), most involve a delay in the delivery of the goods by the seller.[45] In a proper case, the buyer may also recover under sub-

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sonable manner); Acme Pump Co., Inc., v. National Cash Register Co., 337 A.2d 672, 677 (Conn. 1974)(section 2-714(2) formula not exclusive measure of damages in breach of warranty cases; loss directly and naturally resulting is measure of damages); District Concrete Co., Inc. v. Bernstein Concrete Corp., 418 A.2d 1030, 1036 (App. D.C. 1980)(citing § 2-714(1) for the recovery of damages); Cambern v. Hubbling, 238 N.W.2d 622, 625 (Minn. 1976)(section 2-714(2) not exclusive formula for breach of warranty damages). *See generally* G. WALLACH, THE LAW OF SALES UNDER THE UNIFORM COMMERCIAL CODE 10.03 (1981)(commercial law yet to discuss question of what claims fall under general rule of § 2-714(1)); J. WHITE & R. SUMMERS, *supra* note 4, at 376 (general rule is that damages determined in any reasonable manner).

[40] Fargo Mach. & Tool Co. v. Kearney & Treacker Corp., 428 F. Supp. 364, 382-83 (E.D. Mich. 1977). The court awarded buyer the value (contract price) of an optional part which was not delivered and of another such part which the record showed to be worthless. *Id.* The case is an interesting example of a court carefully sifting through the record to find any evidence of probative value to support a damage award. A lawyer should never expect a court to voluntarily suffer such an imposition.

[41] *Id.*

[42] *Id.*

[43] *See supra* notes 1-30 and accompanying text.

[44] *See* Special Project, *supra* note 30, at 104-128.

[45] *See* Jay V. Zimmerman Co. v. General Mills, Inc., 327 F. Supp. 1198, 1203 (E.D. Mo. 1972)(delay in requiring inpack premiums for cereal); Elar Inv., Inc. v. Southwest Culvert Co., Inc., 676 P.2d 659, 661 (Ariz. 1983)(delay in providing prefabricated steel for construction of townhouse units); Franklin Grain & Supply Co. v. Ingram, 44 Ill. App. 3d 730, 358 N.E.2d 922, 923 (1976)(failure to deliver and spread fertilizer at agreed-upon time); Fertico Belgium S.A. v. Phosphate Chemicals Export Ass'n, Inc., 70 N.Y.2d 76, 517 N.Y.S.2d 465, 467, 510 N.E.2d 334, 335 (1987)(delay in delivery to buyer of fertilizer

section (3) incidental[46] and consequential[47] damages caused by the seller's delay in delivery. Thus, in *Franklin Grain and Supply Co. v. Ingram* the buyer was held entitled to recover consequential damages for a reduced crop yield when the seller's late delivery of fertilizer caused it to be spread too late for maximum effectiveness.[48] Similarly, in *Elar Instruments, Inc. v. Southwest Culvert Co.*, the buyer was allowed recovery for consequential damages in the nature of additional charges paid to a third party for financing the goods when the seller was over six months late with its tender.[49]

Commentators have suggested that subsection (1) might be applicable where the seller tenders less than the quantity of goods called for by the contract.[50] The buyer should certainly be allowed damages for the quantity deficiency. However, since such damages are not for accepted goods, section 2-714 would not technically be applicable. In most such cases the buyer will either cover for the deficiency and base his damage claim on section 2-712 or will bring action under section 2-713 for the market/contract price differential. However, if the going market price for the goods is below the contract price, the buyer will be able to prove no damages under sections 2-712 and 2-713. In most such cases, the buyer is well advised to reject the entire shipment of goods, which he is entitled by the Code to do,[51] and to purchase substitutes elsewhere at the lower price. However, if the buyer has an immediate need for the contracted goods, for example to supply a resale customer, good business practice, as well as the duty to mitigate damages, may require him to accept

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on international market).

[46] *See* District Concrete Co., Inc. v. Bernstein Concrete Corp., 418 A.2d 1030, 1038 (App. D. C. 1980)(cost of field overhead in repairing damages caused by defective concrete was properly included in damage award).

[47] *See Elar Inv., Inc.*, 676 P.2d at 662-63 (buyer entitled to recover finance charges incurred an result of seller breach); *Franklin Grain & Supply Co.*, 358 N.E.2d at 925 (1976)(late delivery of fertilizer was non-conforming, buyer entitled to recover consequential damages).

[48] *Franklin Grain & Supply Co.*, 358 N.E.2d at 915.

[49] *Elar Investments*, 676 P.2d at 662-63.

[50] W. HAWKLAND, *supra* note 28 at 374-76.

[51] U.C.C. §§ 2-307 & 2-601 (1978). *See* U.C.C. § 2-717 (upon notifying seller of intention, buyer may deduct all or part of damages resulting from breach of contract from any part of price still due under same contract).

the deficient tender. If he does, he should be allowed an offset against the contract price for the deficiency. However, the proper Code provision for calculating the loss is section 2-711(1), which would allow the buyer a pro rata refund of the purchase price for the undelivered goods.[52]

As subsection (1) to section 2-714 has been rarely utilized, it is difficult to conceive of cases for its application. Nevertheless, the subsection is broadly written and holds promise for the creative lawyer.

B. Damages for Breach of Warranty - Section 2-714(2)

Subsection (2) of section 2-714 provides a value differential formula for breach of warranty cases. It states:

> The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted . . . ."[53]

This formula applies "unless special circumstances show proximate damages of a different amount"[54] or unless the parties by agreement have stipulated damages of a different amount under section 2-718 or have otherwise limited the remedy for breach of warranty under section 2-719.[55]

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[52] *Id.* § 2-711(1)(1978).

[53] *Id.* § 2-714(2).

[54] *Id.* § 2-714 (2). Comment 3 to § 2-714 states:

> Subsection (2) describes the usual standard and reasonable method of ascertaining damages in the case of breach of warranty, but it is not intended as an exclusive measure. It departs from the measure of damages for non-delivery in utilizing the place of acceptance rather than the place of tender. In some cases the two may coincide, as where the buyer signifies his acceptance upon the tender. If, however, the non-conformity is such as would justify revocation of acceptance, the time and place of acceptance under this section is determined as of the buyer's decision not to revoke.

Id.

[55] For cases authorizing damages under § 2-714(2) following finding by court that agreed remedy had failed of its essential purpose under § 2-719(2), see Delhomme Indus., Inc. v. Houston Beechcraft, Inc., 735 F.2d 177, 184 (4th Cir. 1984)(limited remedy failed because seller failed to correct defects within reasonable time); Massey-Ferguson, Inc. v. Laird, 432 So. 2d 1259, 1264 (Ala. 1983)(buyer's damages not limited since numerous attempts to repair combine were made over extended period of time); Walker Ford Sales v. Gaither, 578 S.W.2d 23, 26 (Ark. 1979)(limited remedy failed since machinery could

The Code provides for four types of warranties the breach of which can give rise to an action under section 2-714: (1) warranties of title and against infringement (section 2-312); (2) express warranties (section 2-313); (3) implied warranties of merchantability (section 2-314); and (4) implied warranties of fitness for a particular purpose (section 2-315). To establish a warranty claim, the buyer must prove the existence of a warranty, a breach and a causal link between the breach and the alleged harm.[56] Once it is determined that a buyer is entitled to damages under section 2-714(2), two rather difficult questions immediately present themselves. First, how does one measure the value of the goods as accepted and their value had they been as warranted? Second, to what extent, if at all, is the value measurement subjective (according to the particular needs of the plaintiff buyer) as opposed to objective in terms of a general market measurement?[57] These questions are made difficult because, as one court succinctly put it:

> There is no code definition of value applicable to [section 2-714(2)]. The general definition of value in [section] 1-201(44) obviously has no relevance here since it looks to the characteristics of an entirely different transaction. The value criterion in [section 2-714(2)] is confusing because it serves two very different functions. One use of value is to measure the utility of the defective goods received. Value also serves to define the other component in the compensation equation, the value of the goods as warranted with which the goods as delivered are to be compared.[58]

The concept of value in the law of damages has long presented problems. Professor Corbin put the matter this way:

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not be repaired); Cayuga Harvester, Inc. v. Allis-Chalmers Corp., 95 A.D.2d 5, 465 N.Y.S.2d 606, 611-12 (1983)(finding that limited warranty failed of essential purpose freed buyer to pursue other remedies); Osburn v. Bendix Home Sys., Inc., 613 P.2d 445, 449-59 (Okla. 1980)(same). *But see* Belfont Sales Corp. v. Green Indus., Inc., 112 A.D.2d 96, 491 N.Y.S.2d 652, 654-55 (1985)(contractual provision barring claims for incidental and inconsequential damages not unconscionable).

[56] Peterson v. Bendix Home Systems, Inc., 318 N.W.2d 50, 52-53 (Minn. 1982). For a very helpful short discussion of Code warranties, see J. WHITE & R. SUMMERS, *supra* note 4, at 325-74.

[57] *See* J. WHITE & R. SUMMERS, *supra* note 4, at 377.

[58] Carlson v. Rysavy, 262 N.W.2d 27, 30-31 (S.D. 1978).

> The valuation of a promised performance is far from a simple matter, both because the concept of value is itself variable and because the performances that may be promised are capable of endless variety. As used [to calculate damages], the value of a promised performance or other subject matter is the amount of money that can be obtained or must be given in exchange therefor by bargaining. This amount is not single, definite, or unchangeable. It varies with the persons who bargain and with the time, place, and circumstances under which they bargain. The subject matter to be valued may be one the like of which is a common subject of exchange or one that is not. There may be an established market place for the purchase and sale of such a commodity or there may be none. The amount of money that can be obtained in exchange by a seller is not identical with the amount that must be paid by one who wishes to buy.[59]

The courts historically and under the Code have preferred to calculate value using objective measures such as contract or market price over trying to determine the subjective value of the goods to an individual buyer. The preference is understandable and almost always leads to fair results in commercial settings where subjective and objective values will usually be equal. For example, a commercial buyer holding goods for resale is concerned only with the price he will receive on the market and has no emotional attachment to the goods.[60]

In many cases the courts have avoided the two "value" measurements in subsection (2) by simply allowing the buyer to recover costs of repairing the goods. In these cases, the cost of repairs is accepted as valid evidence of the difference in the values (whatever they may be) of the goods as warranted and as accepted. However, repair cost will not always provide an accurate measurement of the value differential. Where the repair fails to bring the goods up to their warranted value, an upward adjustment in damages must be made. Occasionally, repairs will increase the value of the goods to an amount which exceeds their warranted value. In such a case, a downward adjustment of damages is necessary.[61]

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[59] A. Corbin, Corbin On Contracts § 1004, 38-39 (1964).

[60] For helpful discussions of "value" in the law of damages, see A. Corbin, *supra* note 59, at § 1004 (1964) and C. McCormick, Handbook on the Law of Damages §§ 43-49 (1935).

1. Cost of Repair

Cost of repair to bring the goods to their warranted condition has been widely recognized by the courts as a valid measure of a buyer's general damages under section 2-714.[62] While a few courts have erroneously rejected repair costs in favor of measuring damages under the amorphous "value" standards of subsection (2),[63] the overwhelming judicial consensus has been that such costs are strong evidence of the difference between the value of the goods as accepted and their value as warranted.[64] Occasionally, the courts have awarded costs of repair in warranty cases under the "non-conformity of tender" provision of subsection (1)[65] and under the "special circumstances" exception of subsection (2).[66]

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[61] *See infra* notes 62-111 and accompanying text (discussion of adjustment both upward and downward).

[62] *See, e.g.*, Continental Sand & Gravel, Inc. v. K&K Sand & Gravel, Inc., 755 F.2d 87 (7th Cir. 1985)(district court properly computed damages in using repair cost formula relative to matter of bringing conveyed equipment up to warranted condition); Custom Automated Mach. v. Penda Corp., 537 F. Supp. 77, 84 (N.D. Ill. 1982)(section 2-714 value difference can be computed by reference to cost of repairing goods to conform to warranty standards); Industrial Graphics, Inc. v. Asahi Corp., 485 F. Supp. 793, 802 (D. Minn. 1980)(same).

[63] *See* Valley Datsun v. Martinez, 578 S.W.2d 485, 490(Tex. Ct. App. 1979)(measure of damages is difference in market value of condition at delivery and market value in condition in which it should have been delivered according to contract); Melody Home Mfg Co. v. Morrison, 502 S.W.2d 196, 202 (Tex. Ct. App. 1973)(measure of damages is difference between value of goods as accepted and value as warranted); Chaq Oil Co. v. Gardner Mach. Corp., 500 S.W.2d 877, 878 (Tex. Ct. App. 1973)(measure of damages is difference in market value of equipment as delivered and as warranted).

[64] *See* Winchester v. McCulloch Bros. Garage, 388 So.2d 927, 928-29 (Ala. 1980)(where goods are repairable, cost to repair is useful measure of difference in values as warranted and as delivered); Bendix Home Sys., Inc. v. Jessop, 644 P.2d 843, 847 (Alaska 1982)(absent evidence of actual value, only basis for awarding damages is cost of repair); Downs v. Shouse, 501 P.2d 401, 406 (Ariz. Ct. App. 1972)(expenditures to bring goods into conformity with warranty may be measure of damages); Crest Container Corp. v. R.H. Bishop Co., 111 Ill. App. 3d 1068, 67 Ill. Dec. 727, 445 N.E.2d 19, 24-25 (Ill. App. Ct. 1982)(practical measure of damages is cost to repair to qualify warranted condition); Midland Supply Co., Inc. v. Ehret Plumbing & Heating Co., 108 Ill. App. 3d 1120, 64 Ill. Dec. 601, 440 N.E.2d 153, 157 (1982)(same).

[65] *See* Fargo Mach. & Tool Co. v. Kearney & Trecker Corp., 428 F. Supp. 364, 385 (E.D. Mich. 1977)(damages may be in amount of reasonable expenditures to make goods conform to warranty); Lidstrand v. Silvercrest Indus., 623 P.2d 710, 715 (Wash. Ct. App. 1981)(costs of repair are permissible damages for breach of warranty).

The ease with which repair costs can be ascertained and proved at trial[67] has caused the courts to regard them as preferable evidence[68] of damages as opposed to more uncertain and often subjective evidence as to value.[69] It is often quite difficult for a buyer to prove value with requisite certainty, both as to the goods as accepted and as warranted.[70] Nevertheless, cost of repairs is only evidence of, and thus not dispositive of, the value differential measurement called for by subsection (2).[71] Unless special circumstances justify a different damage measurement, breach of warranty damages for accepted goods must always be measured by the difference between the value of the goods accepted and the value they would have had if they had been as warranted.[72] The obvious cases in which cost of repair does not accurately establish the value differential are those in which the repaired goods are worth less than their warranted value and those in which they are actually worth more. In the former case, the buyer should recover additional damages represented by the value differential between the goods as warranted and as repaired. In the latter case, the seller should be entitled to an offset against the cost of repairs for the enhanced value of the goods.[73]

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[66] *See* R.W. Murray Co. v. Shatterproof Glass Corp., 758 F.2d 266, 272 (8th Cir. 1985)(special circumstances show that plaintiff suffered "proximity damages" of different amount than that which is ordinarily recoverable); City of New York v. Pullman, Inc., 662 F.2d 910, 918 (2d Cir. 1981)(appropriate measure of damages is cost of converting non-conforming goods into goods as warranted). *But see* Wright v. T & B Auto Sales, Inc., 325 S.E.2d 493, 498 (N.C. Ct. App. 1985)(cost of repair not accurate since defective part caused total destruction of engine; proper measure is cost of new engine under "special circumstances" doctrine).

[67] *See generally* Hahn v. Ford Motor Co., 434 N.E.2d 943, 955 (Ind. Ct. App. 1982)(cost of repairs is often utilized to ascertain difference in value between goods accepted and warranted).

[68] *See, e.g.,* Tartar v. Monark Boat Co., 430 F. Supp. 1290, 1293 (E.D. Mo. 1977)(cost of repair provides stronger measure of damages), *aff'd*, 574 F.2d 984 (8th Cir. 1978).

[69] *See* Industrial Graphics,Inc. v. Asahi Corp., 485 F. Supp. 793, 802 (D. Minn. 1980)(cost of repairs is reliable measure of value differential where it restores goods to their value as warranted); Curtis v. Murphy Elevator Co., 407 F. Supp. 940, 950 (E.D. Tenn. 1976)(cost of repair appropriate measure of value differential where plaintiff would be made whole by converting AC-type elevators to DC-type); Bendix Home Sys, Inc. v. Jessop, 644 P.2d 843, 847 (Alaska 1982)("absent evidence, such as appraisal, of the actual value of the home, the only basis for awarding damages is the cost of repairing the home . . ."); S.H. Nevers Corp. v. Husky Hudraulics, Inc., 408 A.2d 676, 680 (Me. 1979)(cost of repair "yardstick" of value differential). *See generally* J. White and R. Summers, *supra* note 4 at 377 (discussing proof of value differential).

[70] *See generally* Winchester v. McCulloch Bros. Garage, 388 So. 2d 927, 928-29 (Ala. 1980)(since it is often difficult to ascertain value of goods as delivered, where goods are repairable, cost to repair is useful measure of difference in values).

[71] W. Hawkland, Uniform Commercial Code Series § 2-714:04 (1982). Note that cases utilizing costs of repair or replacement as measure of general damages will invariably be a breach of warranty case as opposed to other "nonconformity of tender" cases.

[72] *Id.*

Where the costs of repair fail to bring the goods to their fair value as warranted, most courts recognize the necessity of making an upward adjustment in order to fully compensate the buyer under section 2-714.[74] The other side of the coin is the possibility of over-compensating a buyer where the repairs enhance the value of the goods above the warranted value.[75] In such cases, the Code's provision on compensation and liberal administration of remedies[76] requires that the amount of recovery (repair costs) be adjusted downwards by the amount of the value enhancement.[77] Otherwise, the buyer will be over-compensated by the amount of the enhancement.[78] Repairs will enhance the value of goods usually only in cases in which the goods were sold used or in which the defects did not manifest themselves until long after the buyer has taken delivery of the goods.[79]

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[73] Soo Line Railroad Co. v. Fruehauf, 547 F.2d 1365 (8th Cir. 1977). Soo Line was the buyer of 500 railroad hopper cars which developed structural cracks within months of the delivery date despite an estimated 40-year useful life. *Id.* at 1367. Soo Line repaired the hopper cars after the seller [Fruehauf] refused to do so. *Id.* at 1368. In Soo Line's subsequent suit for damages, it argued that the repaired and patched hopper cars had less value than properly manufactured cars. *Id.* The Eighth Circuit quoted with approval the following jury instructions given by the trial court:

> The measure of damages is, generally speaking, the difference between the fair market value of the cars as accepted by Soo Line, and the value they would have had if they had not been deficient in the particulars in which you found them deficient. This is called the difference or diminution in value approach.
>
> . . . .
>
> If you find that the repair of the cars restored the cars to substantially the same condition as they would have been in if properly manufactured, the difference or diminution value is the same as the reasonable cost of repairing the cars.
>
> So, if the repair costs actually restored them then the repair cost would equal the diminution in value. However, if you find that the repair of the cars did not restore them to substantially the same condition as they would have been if properly manufactured, then the difference or diminution in value is the reasonable cost of repair, plus the difference between the fair market value of the covered hopper cars if they had been manufactured without faults or defects, and the fair market value of the repairs.
>
> The total figure, however, cannot exceed the difference between the fair market value as accepted, and the fair market value in the defective condition you find.
>
> . . . .
>
> Therefore, if you find that the repairs of the cars placed the cars in a better condition than they would have been at the time of acceptance if they had been properly manufactured, then the difference or diminution in value recoverable by the plaintiffs is the difference between the fair market value of the covered hopper cars as accepted by Soo Line and the fair market value they would have had if Magor [defendant] had manufactured them properly. So, Soo Line in this situation would not be able to recover the full amount spent for repairs.

Id. at 1378.

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[74] *See, e.g.*, Stutts v . Green Ford, Inc., 47 N.C. App. 503, 267 S.E.2d 919, 926 (1980). In *Stutts*, the seller was able to repair all of the defects except one, a persistent oil leak. *Id.* at 925. The court ascertained damages by awarding the difference in the fair market value of the truck in its condition at the time and place of acceptance, increased by the value of repairs and replacements made by the seller, and its fair market value had it been as warranted. *Id.* This calculation, the court correctly explained, allowed the plaintiff "to recover damages compensating him for the loss in value due to the persistent oil problem, while preventing him from receiving windfall damages for defects which were subsequently successfully repaired." *Id.* *See also* Hartzell v. Justus Co., Inc., 693 F.2d 770, 773, (8th Cir. 1982)(proper measure of damages is cost of repairs plus decrease in market value still existing after all repairs have been completed); Carlson v. Rysavy, 262 N.W.2d 27, 30-32 (S.D. 1978)(measure of damages is difference between warranted value and actual value). *But see* Smart v. Tidwell Industries, Inc., 668 S.W.2d 605, 609 (Mo. Ct. App. 1984)(when evidence shows cost of repair or restoration of property to its represented condition to be significantly less than value differential, former is proper measure of damages); Cundy v. International Trencher Serv., Inc., 358 N.W.2d 233, 240-41 (S.D. 1984)(where trencher repaired for $15,000 post-trial, $20,000 jury award based on value differential was incorrect); *cf.* Ehlers v. Chrysler Motor Corp.88 S.D. 612, 226 N.W.2d 157, 162 (S.D. 1974)(jury verdict of $3,500 upheld despite competent evidence that entire defective transmission could have been replaced for approximately $400).

[75] *See supra* note 73 and accompanying text (discussing two occasions where repair measure produces wrong result).

[76] U.C.C. § 1-106 (1978).

[77] *Id.*

[78] *See, e.g.*, Soo Line R.R. Co. v. Freuhauf Corp., 547 F.2d 1365, 1371 (8th Cir. 1977)(court reduced recover by amount of enhancement); Community Television Services, Inc. v. Dresser Indus., Inc., 435 F. Supp. 214, 219 (same); Newman v. Spector Wrecking & Salvage Co., 490 S.W. 875, 882 (Tex. Ct. App. 1973)(same). *But see* General Supply & Equip. Co. v. Phillips, 490 S.W.2d 913 (Tex. Ct. App. 1972). This was an early case which failed to consider buyer's beneficial use of the goods in its calculation of damages. *Id.* at 915. The buyer had purchased roofing panels for his four greenhouses. *Id.* The panels were warranted to last for five to seven years. *Id.* The panels were placed on greenhouse no. 2 in 1966; on no. 4 in 1967, and on nos. 1 and 3 in either 1967 or 1968. *Id.* The panels on greenhouses 2 and 4 were replaced in 1969 when the buyer discovered the panels to be defective as evidenced by a premature darkening. *Id.* at 917. This darkening prevented adequate sunlight from entering the greenhouses, and resulted in the loss of plants and a decline in the buyer's business. *Id.* The buyer ultimately sold the green-

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houses in 1970. *Id.* The court held:

> In the instant case the ordinary measure of damages for breach of warranty stated in [section 2-714(2)] is not applicable because of special circumstances showing proximate damages of a different amount. The proximate damages in this case consist of incidental and consequential damages as provided in [section 2-715].
>
> . . .
>
> [T]he jury found that the cost of installing the defective paneling amounted to $16,305.00 and that the cost of replacing the defective paneling on two of the greenhouses amounted to $10,385.00. The judgment awarded [buyer] a recovery for both amounts. This constitutes an erroneous measure of damage for the reason that it operates as a windfall in favor of [buyer] and allows a double recovery. Under this measure of damages [buyer] would be fully reimbursed for the defective paneling and would be paid for a new roof on two of the greenhouses free of any cost. As stated above, we think the proper measure of damages would be the cost of replacing the defective panels on all four greenhouses.
>
> As we view the record, there is no way that judgment can be rendered because the incidental damages, i.e., the reasonable cost of replacing the defective paneling on all four greenhouses is a matter which has never been ascertained by the jury.

Id. at 920-22.

[79] *See, e.g.*, Newman v. Spector Wrecking & Salvage Co., 490 S.W.2d 875, 877 (Tex. Ct. App. 1973)(involving purchase of used equipment). In *Newman*, the equipment was inoperable and thus not as warranted. *Id.* at 876. The buyer maintained that the equipment was worthless as accepted and was awarded damages equal to the cost of new replacement equipment. *Id.* On appeal, the seller argued that the judgment was excessive. *Id.* The court agreed and remanded the case for a redetermination of damages. *Id.* at 878. The court reasoned that a recovery for the full cost of repair would clearly put the plaintiff in a better position than he would have occupied by performance, because the court could "take judicial knowledge of the fact that there is a difference in value between a used and a new item of mechanical equipment." *Id.* The court also expressed concern that the recovery allowed by the trial court exceeded the contract price for the used equipment. *Id.* On this point, the court misfocused. The concern should have been whether repair costs exceeded the value as warranted. The contract price is not dispositive of the value of the goods as warranted. *See infra* notes 112-132 and accompanying text. *See also* Community Television Service, Inc. v. Dressed Indus., Inc., 435 F. Supp. 214 (D.S.D. 1977). Here, the court reduced the buyer's recovery for replacement of a television and radio broadcasting tower which had collapsed during a blizzard. *Id.* at 214. The tower was totally destroyed, and buildings beneath the tower were damaged. *Id.* The buyer had used the tower for some time prior to its destruction. *Id.* The jury awarded damages of $1,385,001.61 for the seller's breach of warranty. *Id.* The court held that under the circumstances of the case the award would over-compensate the buyer unless damages were reduced by a reasonable depreciation for the buyer's beneficial use of the tower prior to its destruction. *Id.*

Another way in which an award of repair costs will overcompensate a buyer is where the costs exceed the value of the goods as warranted.[80] Under the value differential formula of section 2-714(2) the value of the goods as warranted is by definition a ceiling on the buyer's general damages recovery.[81] How a court chooses to measure this "value" is of obvious importance.[82] Unfortunately, many courts have assumed that the value of the goods as warranted is always reflected by the contract price for the goods.[83]

A recent case exposing the flaw in using the purchase price as the ceiling for recovery under section 2-714(2) is *Continental Sand & Gravel v. K & K Sand & Gravel, Inc.*,[84] which involved the purchase of defective equipment for a price of $50,000.[85] The buyer sued for a breach of warranty and recovered repair costs in excess of $104,000.[86] The court on appeal affirmed the verdict over vigorous protest by the defendants that under no circumstance could recovery exceed the purchase price of $50,000.[87] The court noted that it was not unusual for damages in a breach of warranty case to exceed the purchase price of the goods.[88] The court said, "this result is logical, since to limit recoverable damages by the purchase price, as defendants suggest, would clearly deprive the purchaser of the benefit of his bargain in cases in which the value of the goods as warranted exceeds that price."[89]

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[80] *See supra* note 61 and accompanying text.

[81] *See* U.C.C. § 1-106 (1978).

[82] *Id.*

[83] *See, e.g.*, Winchester v. McCulloch Bros. Garage, Inc., 388 So. 2d 927, 930 (Ala. 1970) where the jury awarded $20,000 to the buyer of a defective vehicle. *Id.* On appeal, the court characterized the verdict as clearly excessive. *Id.* The court said:

> In the unlikely event the truck could not be repaired and had no salvage value, the difference in the value of the truck as accepted and its value as warranted can be no more than $8,225.00, the cost of the truck. Since no includable consequential damage was shown, the total award could not exceed $8,225.00, and the jury award of $20,000 was certainly improper.

Id.

[84] 755 F.2d 87 (7th Cir. 1985).

[85] *Id.* at 89.

[86] *Id.* at 94.

[87] *Id.*

[88] *Id.* at 95. City of New York v. Pullman, Inc., 662 F.2d 910, 916 (2d Cir. 1981)(party entitled to what bargained for). The fact that fair market value rather than contract price is a more accurate measure of "value" as warranted under section 2-714(2) is fully discussed *infra* note 112-132.

When costs of repair are accepted as evidence of the value differential under section 2-714(2) there is no requirement that the buyer have actually expended the monies for repair or, apparently, that he introduce evidence that the repairs will be made.[90] In such cases, the courts have allowed the costs to be proved by expert testimony in the form of repair estimates.[91] Presumably the estimates should be based on repair costs at the time and place of acceptance, rather than at trial, because the costs are being received as evidence of value differential at the earlier time.[92] At least one case, however, has held that, where repair costs have risen substantially in the interim between the times of acceptance and trial, the repair costs can be measured at the time of trial.[93] The court emphasized that liability for the repairs was sharply contested by the seller and, thus, the buyer could not make an informed decision on whether to proceed with the repair work until it knew who would pay the bill.[94] The court reasoned that economic considerations might require the buyer to forego the repair work if the seller was not obligated to pay for it.[95] On this basis, the court rejected the seller's argument that the buyer had wrongfully failed to mitigate damages.[96] The court was satisfied that the recovery compensated the buyer by placing it in the position it would have occupied had the seller performed its repair obligations.[97] The court was apparently of the opinion that the increase in repair costs were consequential damages recoverable under subsection (3) rather than general damages under subsection (2).[98] The court said that the increased costs resulting from normal inflation were a reasonable and foreseeable consequence of the seller's breach of its obligation to repair.[99] The buyer was thus allowed a recovery in excess of $10,000 for the increase in costs.[100] The court's conclusion would appear correct only if the evidence showed that the buyer actually planned to make the repairs upon recovery of their costs from the seller and if economic considerations actually did reasonably warrant the buyer's not previously making the repairs.[101] In such a case, however, the buyer's recovery of

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[89] *Continental Sand & Gravel*, 755 F.2d at 95.

[90] *See* Sellinger v. Freeway Mobile Home Sales, Inc., 110 Ariz. 573, 521 P.2d 1119, 1122 (1974)(permissible to award damages based upon estimate of repair costs); Teledyne Indus. v. Patron Aviation, Inc., 161 Ga. App. 596, 288 S.E.2d 911, 915 (1982)(evidence of repair estimate allowed); Chrysler Corp. v. Wilson Plumbing Co., 132, Ga. App. 435, 208 S.E.2d 321, 325 (1974)(recovery not allowed to exceed estimate of cost of repair); Southern Concrete Products Co. v. Martin, 126 Ga. App. 534, 191 S.E.2d 314, 317 (1972)(testimony of expert supported claim for repair costs); Jones v. Abriani, 169 Ind. App. 556, 350 N.E.2d 635, 647 (1976)(proof of potential repair costs permissible where actual damages were not made).

[91] U.C.C. § 2-714 (1977).

[92] *Id.* at comment 3. It should be kept in mind that, according to U.C.C. § 2-714, comment 3 (1977): "If, however, the non-conformity is such as would justify revocation of acceptance, the time and place of acceptance under this section is determined as of the buyer's decision not to revoke." *Id.*

[93] Camrosa County Water Dist. v. Southwest Welding & Mfg. Co., 49 Cal. App. 3d 951, 123 Cal. Rptr. 93, 96 (1975).

[94] *Camrosa County Water Dist.*, 123 Cal. Rptr. at 96.

[95] *Id.*

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[96] *Id.*

[97] *Id.*

[98] *Id.*

[99] *Id.* at 98.

[100] *Id.*

[101] *See* R.W. Murray Co. v. Shatterproof Glass Corp., 697 F.2d 818, 825 (8th Cir. 1983)(since seller's consequential damage disclaimer was held invalid, court need not determine whether repair damages were direct or consequential); *cf.* Duff v. Bonner Bldg. Supply, Inc., 103 Idaho 432, 649 P.2d 391, 396 (1982)(cost of replacement paneling held recoverable under § 2-714(2) and additional costs of removing old paneling and installing new paneling held recoverable as incidental damages under § 2-715(1)).

The *R.W. Murray* case is also noteworthy for its award of anticipatory damages. Murray was a general contractor who sued Shatterproof for breach of warranty in the sale of glass panels sold in 1974 to one of its subcontractors, Boain. *R.W. Murray*, 697 F.2d at 820-21. The panels had already been installed in the office building Murray was constructing when a number of the panels developed moisture accumulation between their panes. *Id.* After this suit was voluntarily dismissed, the owner of the office building and Murray then sued Shatterproof for breach of warranty. *Id.* Expert witnesses testified that it was likely that the remainder of the panels sold would ultimately experience the same premature seal failure. *Id.* It was further shown that there was no supplier who could match the original panels and that the building was taking on an unsightly checkerboard appearance. *Id.* In light of the anticipated failure of all of the panels and in order to restore the building to a "commercially tolerable appearance," the cost of replacing all panels was awarded. *Id.*

Nevertheless, courts frequently permit buyers to estimate repair costs or to use expert testimony as to the cost of repair. *See, e.g.*, Curtis v. Murphy Elevator Co., 407 F. Supp. 940 (E.D. Tenn. 1976)(court chose between conflicting testimony as to estimated cost of repairing elevators); Sellinger v. Freeway Mobile Home Sales, Inc., 110 Ariz. 573, 521 P.2d 1119 (1974)(expert testimony of repair estimate to mobile home); Chrysler the increased costs need not be classified as consequential damages but could be recoverable as general damages under the "special circumstances" exception in subsection (2).[102] Nevertheless, the question of whether the increased repair costs are consequential or direct damages will usually become important only in cases in which the seller has excluded liability for consequential loss.[103]

Occasionally, the buyer will decide to repair the goods himself rather than contracting for the repairs with a third party. In such a case, there is no reason why the buyer should not be allowed recovery for his out-of-pocket expense and a reasonable profit for his time and efforts.[104] His recovery, however, should be reasonably limited to the amount that an independent party would have charged for the repair work. As one court explained:

> If another contractor had been hired to perform the repair work it would have been entitled to a profit. [The seller] should not benefit by depriving the [buyer] of a profit on work it was required to perform only because of [the seller's] breach of warranty.[105]

The court designated the following elements as proper items for calculating the buyer's costs of repairing a defective thermaforming machine to meet warranty standards:

(a) maintenance employee time - $9,522 (529 downtime hours x $18/hour);
(b) assistance and parts from outside contractors - $67,566;
(c) parts from the buyer's inventory - $500, and

Corp. v. Wilson Plumbing Co., 132 Ga. App. 435, 208 S.E.2d 321 (1974)(estimated cost of repairing car).

[102] *See* Southern Concrete Products Co. v. Martin, 126 Ga. App. 534, 191 S.E.2d 314 (1972)(court resorted to "special circumstances" clause of § 2-714(2) in awarding cost of sandblasting mud-stained bricks); General Supply & Equipment Co. v. Phillips, 490 S.W.2d 913 (Tex. Civ. App. 1972)(cost of replacing greenhouse paneling).

[103] Robert T. Donaldson, Inc. v. Aggregate Surfacing Corp. of Am., 366 N.Y.S.2d 194, 196, 17 375, 377 (N.Y. App. Div. 1975). *See also* Midland Supply Co. v. Ehret Plumbing & Heating Co., 440 N.E.2d 153, 157, (Ill. App. Ct. 1982)(labor cost incurred by defendant in replacement of parts recoverable); Delano Growers Coop. Winery v. Supreme Wine Co., Inc., 473 N.E.2d 1066, 1077, (Mass. 1985)(cost of labor for repairs made is recoverable).

[104] Custom Automated Mach. v. Pendo Corp., 537 F. Supp. 77, 84 (N.D. Ill. 1982).

[105] *Id.*

> (d) addition of twin-sheet capability so as to meet performance standards specified in the contract - $5,000.[106]

The seller argued that the buyer was not entitled to the costs of its maintenance employees' time because there was no evidence that the buyer had hired any additional maintenance personnel or had required its regular employees to work overtime.[107] In rejecting this argument, the court said:

> [T]he cost of [the buyer's] employees' time was part of the cost of repairing a machine that [the buyer] would not have had to repair if it had operated as warranted. Therefore, the costs of maintenance employee time was part of the difference in value between the machine as accepted and as warranted to which [the buyer] is entitled under [section 2-714]. [The seller] may not evade responsibility for a cost stemming from its breach simply because [the buyer] used its own personnel rather than hiring outside maintenance people.[108]

Of course, the defects in the goods may on occasion prove to be unrepairable. In such cases, costs incurred in attempting repairs in no way represent valid evidence of the value differential under section 2-714(2).[109] Nevertheless, the costs should be recoverable as consequential damages if they were incurred in a reasonable attempt by the buyer to mitigate his loss.[110] In such cases, the buyer may additionally recover general damages under subsection (2) if the buyer has introduced evidence of the appropriate value differential or if "special circumstances" in the record show damages of a different amount.[111] To the difficulties of proving such damages we now turn.

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[106] *Id.*

[107] *Id.* at 84 n.9.

[108] *Id. But see* Curtis v. Murphy Elevator Co., 407 F. Supp. 940, 950 (E.D. Tenn. 1976)(cost of unsuccessful repair attempts allowed as direct damages under § 2-714(2)).

[109] *See* Special Project, *Article Two Warranties in Commercial Transactions*, 64 CORNELL L. REV. 30, 109-10 (1978)(attempts to repair recoverable as damages); *see also* J. WHITE & R. SUMMERS, *supra* note 4, at 379 (discussion of items recoverable as consequential damages).

[110] *See supra* note 101.

[111] U.C.C. § 2-714(2)(1977).

2. Value as Warranted

The value differential formula in subsection (2) is expressed as "the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted."[112] The burden is on the buyer to prove the amount of damages under this provision,[113] and this requires that sufficient evidence be presented to establish both the value of the goods as accepted and their value as warranted.[114]

There is no Code definition of "value" applicable to either prong of the formula.[115] This absence of statutory guidance has left to the courts the matter of determining the meaning of "value" under section 2-714.[116] Perhaps "value" should be based

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[112] U.C.C. § 2-714(2)(1978).

[113] Glen O'Brien Movable Partition Co. v. McMullen, 608 S.W.2d 512, 521 (Mo. Ct. App. 1980). Cases indicate that buyers often fail to carry this burden. *See, e.g.*, Smart Chevrolet Co. v. Davis, 262 Ark. 500, 558 S.W.2d 147, 148 (1977)(case reversed and remanded where no evidence of value-differential presented); S.C. Gray, Inc. v. Ford Motor Co., 92 Mich. App. 789, 286 N.W.2d 34, 41 (1979)(evidence of only purchase price and salvage value inadequate to support award for breach of warranty without evidence of actual value of equipment at time of acceptance and it appeared to court to have some value); Wendt v. Beardmore Suburban Chevrolet, Inc., 219 Neb. 774, 366 N.W.2d 424, 428 (1985)(since there was no evidence as to difference in value between new car which had been used as demonstrator and car used as driver training vehicle, there was no evidence upon which award for breach of warranty could be based); Perry v. Lawson Ford Tractor Co., 613 P.2d 458, 465 (Okla. 1980)(evidence presented insufficient for jury to apply value-differential formula for damages); Ellison v. Heritage Dodge, Inc., 320 S.E.2d 716, 718 (S.C. 1984)(nonsuit upheld when evidence of fair market value as warranted presented but no evidence of fair market value as delivered shown). *But see* Fargo Mach. & Tool Co. v. Kearney & Trecker Corp., 428 F. Supp. 364, 383 (E.D. Mich. 1977)(subsection (1) relied upon to award damages to buyer who failed to allege or offer proof on value of goods accepted); Jensen v. Seigel Mobile Homes Group, 105 Idaho 189, 668 P.2d 65, 73 (1983)(if buyers on remand proved unable to show loss in value resulting from beach of warranty, such would constitute "special circumstance" which might enable them to recover on alternative measure of damages).

[114] Carlson v. Rysavey, 262 N.W.2d 26, 30 (S.D. 1978). The one Code definition of "value" in § 1-201(44) does not apply to § 2-714. *Carlson*, 262 N.W.2d at 30.

[115] A. CORBIN, *supra* note 59, at § 1004 (helpful discussion of how courts have defined "value" historically in various damage contexts).

[116] *See* E. Peters, *Remedies for Breach of Contract Relating to the Sale of Goods Under the Uniform Commercial Code: A Roadmap for Article Two*, 73 YALE L.J. 199, 269 (1963), which states:

> The value criterion in 2-714 is confusing because it serves two very different functions. One use of value is to measure the utility of the defective goods

upon the subjective value of the particular goods to the individual.[117] Although it is true that section 2-714 does not use the objective term "market price," as does section 2-713(1), thereby allowing for the flexibility to subjectively compensate the buyer in accordance with the Code's provision on liberal administration of remedies,[118] accurately determining a subjective measure of damages will always give rise to practical problems of proof. Not surprisingly, therefore, the courts have for the most part adopted objective measures such as fair market value, contract price and resale price, as the best indicators of "value" under subsection (2).[119] Rare will be the commercial buyer who can persuasively argue that he subjectively valued the goods in an amount greater than can be objectively established by the mar-

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> received. As such, value is a personalized criterion designed to allow the buyer to offer special evidence of the needs of his own enterprise and resources, to show that the goods accepted are less valuable to him than their market price would otherwise indicate.

Id.; J. White & R. Summers, *supra* note 4, at 382 (discussion of value); A. Corbin, *supra* note 59, at § 1004 (same).

[117] *See* U.C.C. § 1-106 (1978)(remedies to be construed to give buyer expectancy).

[118] *Compare* U.C.C. § 2-713(1)(1978)(measure of damages is difference between market price and contract price) *with* § 2-714 (no reference to market price). Courts have generally applied market value to determine damages. *See* T.J. Stephenson & Co. v. 81, 193 Bags of Flour, 629 F.2d 338, 367 (5th Cir. 1980)(measure of damages established by comparison of market values); Cox Motor Car Co. v. Castle, 402 S.W.2d 429, 431 (Ky. App. 1966)(same); Vreeman v. Davis, 348 N.W.2d 756, 758 (Minn. 1984)(same); Williams v. Hyatt Chrysler-Plymouth, Inc., 48 N.C. App. 308, 269 S.E.2d 184, 189 (1980)(same); Raye v. Fred Oakley Motors, Inc., 646 S.W.2d 288, 290 (Tex. Ct. App. 1983)(same); *Ellison*, 320 S.E.2d at 717 (same). *But see* Puritan Mfg., Inc. v. I. Klayman & Co., 379 F. Supp. 1306, 1314 (E.D. Penn. 1974)(damages equal value as warranted less value to buyer as delivered); Schatz Dist. Co. v. Olivetti Corp. of Am., 647 P.2d 820, 825 (Kan. Ct. App. 1982)(value to buyer zero thus damages equal value as warranted); Louis DeGidio Oil & Gas Burner Sales & Service v. Ace Eng'g Co., 225 N.W.2d 217, 222 (Minn. 1974)(same); *Raye*, 646 S.W.2d at 290 (generally actual damages are difference in market value as warranted versus market value as delivered but exception exists when defect renders product valueless — then purchase price is appropriate measure of actual damages); Chrysler Corp. v. Schuenemann, 618 S.W.2d 799, 805 (Tex. Civ. App. 1981)(same).

In Warren v. Guttanit, Inc., the case involved defective roofing materials, and the buyer was permitted to recover the contract price of $81,067.50 despite the fact that he had actually paid a lesser amount. Warren v. Guttanit, Inc., 69 N.C. App. 103, 317 S.E.2d 5, 12 (1984). The court reasoned that the difference between the contract price and the amount actually paid was due to the plaintiff's paying the defendant in advance and any benefit resulting therefrom rightfully belonged to the plaintiffs and not to the defendant. *Id.*

[119] J. White & R. Summers, *supra* note 4, at 383.

ket. In the rare case, however, the "special circumstances" exception in subsection (2) would permit the buyer to base valuation on more subjective criteria.[120] The contract price for the goods is often employed as evidence of their value as warranted.[121] When the contract price is used to establish this value it should always be the cash price of the goods and not a credit price which would include finance charges. Logically such charges do not reflect the value of the goods but merely represent the cost of money. Although a few courts have permitted finance charges to be included in the determination of the value of the goods as warranted,[122] most courts have restricted evidence of that value to the cash price of the goods.[123] Whenever finance charges are to be allowed as compensable damages, they should be considered consequential damages and be subjected to the specific requirements of section 2-715(2) for the recovery of such damages.[124]

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[120] *See, e.g., Puritan Mfg., Inc.* 379 F. Supp. at 1314 (agreement of parties that purchase price was value of liver and offal chillers had they operated as warranted enforced although warranted value is not necessarily purchase price); Winchester v. McCulloch Bros. Garage, Inc., 388 So. 2d 927, 929 (Ala. 1980)(purchase price is evidence of value of goods as warranted); *Schatz Distrib. Co.*, 647 P.2d at 825 (value as warranted is presumably agreed upon purchase price); *Warren*, 317 S.E.2d at 12 (evidence of purchase price is strong proof of value in condition represented); Perry v. Lawson Ford Tractor Co., 613 P.2d 458, 465 (Okla. 1980)(actual purchase price may be relevant as to the warranted value at the time of acceptance).

[121] J. WHITE & R. SUMMERS, *supra* note 4 at 380, n.18.

[122] *See* Thompson Chrysler-Plymouth, Inc. v. Myers, 48 Ala. 350, 263 So. 2d 893, 897 (1972)(proper to let jury hear evidence as to both cash and credit price in determining value of goods); Elar Investments, Inc. v. Southwest Culvert Co., 139 Ariz. 25, 676 P.2d 659, 662 (1983)(extended financing charges incurred by developer because of delay in delivery of necessary building equipment recoverable as "direct" damages resulting from breach); Burrus v. Itek Corp., 46 Ill. App. 3d 350, 360 N.E.2d 1168, 1172 (1977)(proper to include finance charges in arriving at value of goods as warranted).

[123] *See* Chatlos Sys., Inc. v. National Cash Register Corp., 635 F.2d 1081, 1088 (3d Cir. 1980)(buyer who is awarded lump sum damages could purchase replacement without incurring interest expense, thus recovery which includes interest on original purchase constitutes windfall); Bendix Home Sys., Inc. v. Jessop, 644 P.2d 843, 845 (Alaska 1982)(finance charges represent right not to pay for goods immediately, not increase in value of items purchased); Long v. Quality Mobile Home Brokers, Inc., 271 S.C. 482, 248 S.E.2d 311, 312-13 (1978)(value not increased by finance charges); Bearnard v. Compugraphic Corp., 35 Wash. App. 2d 414, 667 P.2d 117, 121 (1983)(interest is not part of value of goods as warranted but merely cost of money borrowed to buy goods because capital is unavailable to buyer).

[124] *See* Coyle Chevrolet Co. v. Carrier, 397 N.E.2d 1283, 1287 (Ind. Ct. App.

The contract price should not be regarded as alternative evidence to fair market value when the market value is readily ascertainable. However, contract price is a viable and helpful alternative when market value is difficult to establish as, for example, with respect to unique or specially manufactured goods. In such cases, it is fair to assume that the parties themselves, dealing at arms length, have fairly approximated the value of the goods as warranted.[125] However, subsection (2) requires that value be determined as of the time and place of acceptance. The longer the interim between contracting and acceptance the less valid will be the contract price as an indicator of the value of the goods at the time of acceptance.[126] On the other hand, in a stable market, the contract price should reflect market value closely enough to make it uneconomical to establish the actual market value.[127]

1980)(finance charges can be addressed as consequential damage where buyer presents evidence that seller had "reason to know" buyer needed to borrow money in order to complete purchase); *Schatz Distrib. Co., Inc.*, 647 P.2d at 825-27 (proper to award, as consequential damages, interest buyer paid to leasing agency as part of purchase agreement since method of financing known to seller at time of contracting). *But see Long*, 248 S.E.2d at 313 (finance charges incurred by purchaser of defective mobile home not recoverable as consequential damages because they were not "damages naturally and proximately arising out of breach of warranty"); *Barnard*, 667 P.2d at 121 (interest is neither part of value of goods as warranted or consequential damages arising from the seller's breach since interest on money borrowed to purchase goods is incurred by buyer whether goods conform or are defective).

[125] *See, e.g., Ellison*, 320 S.E.2d at 717-18 (original sales price of motor vehicle is evidence of fair market value as warranted); *Raye*, 646 S.W.2d at 290 (market value may be determined by price in excess of market price); *Chrysler*, 618 S.W.2d at 805 (without other proof of market value as warranted, price agreed on by parties may be understood to be market value). *See also* Chatlos Sys., Inc. v. National Cash Register Corp., 670 F.2d 1304, 1306 (3rd Cir. 1982)(evidence of contract price may be relevant to fair market value, but is not controlling). *See* J. WHITE & R. SUMMERS, *supra* note 4 at 380 n.16. *See generally* B. CLARK & C. SMITH, THE LAW OF PRODUCT WARRANTIES ¶ 7.05[2][b], pp. 7-53 (1984).

[126] *See* Special Project, *supra* note 30, at 114-15.

[127] J. WHITE & R. SUMMERS, *supra* note 4, at 380 n.16.

See Special Project, *supra* note 30, at 112-13 (fair market value provides more appropriate standard for establishing warranted value parties with bargain they originally struck). Professor Peters argues that contract price need not reflect market price. Peters, *supra* note 116, at 270.

> If all other formulae speak in terms of contract price, why not this one? A moment's reflection will demonstrate that some sort of adjustment from contract price is needed to preserve for the buyer the benefit of his bargain, whenever the value of the goods as warranted is not the same as the contract price.

Id.

The use of actual market value in a subsection (2) calculation always better serves to insure that the buyer will receive the benefit of his bargain, no more and no less. In cases in which the market price has risen above the market price subsequent to the contract the buyer will thereby be compensated by the good bargain he has made. Conversely, in cases in which the market price has in the interim fallen below the contract price, the buyer will suffer the consequence of his bad bargain and will be denied windfall damages not caused by the seller's breach.[128] The seller's attorney should be alert to the possibility of a buyer's recovery of windfall damages if contract price is introduced as evidence of value when the fair market value of the goods can be readily established.

The going value of goods in regularized markets at a particular time and place is usually quite easily established. Further, when such evidence is not readily available, the Code provides sensible means of alternative proof.[129] Further, the Code liberally permits the use of market quotations,[130] and the use of such quotations, particularly with respect to agricultural commodities, is reflected often in the reported cases.[131] Despite these alternatives, however, it may be necessary for the buyer to procure expert witnesses, such as dealers or the like, to testify as to the warranted value of the goods.[132]

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[128] U.C.C. § 2-723(2) & (3) provide:

> (2) If evidence of a price prevailing at the times or places described in this Article is not readily available, the price prevailing within any reasonable time before or after the time described or at any other place which in commercial judgment or under usage of trade would serve as a reasonable substitute for the one described may be used, making any proper allowance for the cost of transporting the goods to or from such other place.
>
> (3) Evidence of a relevant price prevailing at a time or place other than the one described in this Article offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise.

Id.

[129] U.C.C. § 2-724 provides:

> Whenever the prevailing price or value of any goods regularly bought and sold in any established commodity market is in issue, reports in official publications or trade journals or in newspapers or periodicals of general circulation published as the reports of such market shall be admissible in evidence. The circumstances of the preparation of such a report may be shown to affect its weight but not its admissibility.

Id.

[130] *See generally* Anderson, *Market Based Damages for Buyers Under the Uniform Commercial Code*, 6 THE REV. OF LIT. 1, 33-34 (1987).

[131] *See, e.g.*, B.L. Produce of Ariz., Inc. v. Mims Produce, Inc., 37 Agric. Dec. 201

3. Value as Accepted

Ascertaining the value of the goods as accepted is an appreciably more troublesome endeavor than is establishing the value as warranted.[133] The job is made easier if the non-conforming goods have been resold or if they are at least resalable at a price that can be established. Just as the contract price is often used as the measure of the warranted value of goods, resale price is considered a reasonably accurate measure of the value of the goods as accepted.[134]

Of course, to be admissible as evidence, the resale must have been conducted in a commercially reasonable manner. It has been suggested that the strength of the evidence of resale to establish value will rest upon three criteria.[135] First, the goods must be resold in a reasonably competitive market.[136] Second, the resale must be timely given the nature of the goods involved.[137] For example, goods which depreciate rapidly must be seasonably resold before any substantial change in their condi-

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(1978)(using price of tomatoes reported by Market News Service); Jerome Kantro Co. v. Summers Bros., Inc., 27 Agric. Dec. 129, 5 U.C.C. Rep. Serv. (Callaghan) 135-36 (1968)(official notice taken of Federal Market News Service reports of value of lettuce).

[132] *See* Winchester v. McCulloch Bros. Garage, Inc., 388 So. 2d 927, 928-29 (Ala. 1980)(while purchase price is evidence of value of goods as warranted, it is often difficult to ascertain value of goods as delivered); Vista St. Clair, Inc. v. Landry's Commercial Furnishings, Inc., 57 Or. App. 254, 643 P.2d 1378, 1381 (1982)(real question is actual value of goods delivered).

[133] Special Project, *supra* note 30, at 115-16. In a case that involved defective roofing materials the buyer was permitted to recover the contract price of $81,067.50 despite the fact that he had actually paid a lesser amount. Warren v. Guttanit, Inc., 69 N.C. App. 103, 317 S.E.2d 5, 12-13 (1984). The court reasoned that the difference between the contract price and the amount actually paid was due to plaintiff's paying the defendant in advance any benefit resulting therefrom should rightfully belong to the plaintiffs and not to the defendant. *Id.* at 12.

[134] *See* Special Project, *supra* note 30, at 115 (courts recognize resale price as evidence of actual value).

[135] *Id.* at 115-16.

[136] *Id.* at 115.

[137] *Id.*

tion.[138] Third, the resale purchaser should be made aware of the defective nature of the goods.[139] If these guidelines are adhered to, the presumption should be that the resale price closely approximates the actual fair market value of the non-conforming goods at the time of acceptance.[140]

Since a ready market for defective goods will often not be available, it is not uncommon for the non-conforming goods to still be in the hands of the buyer at the time of trial. In such cases, the buyer is usually permitted to testify as to the fair market value of the non-conforming goods. Even though the buyer is in no sense an expert,[141] he is familiar with the goods and their condition, and the established rule of evidence is that his lack of expertise goes only to the weight of the evidence and not to its admissibility.[142] Such testimony is always to some extent specious, and it becomes especially doubtful when the buyer testifies, as he often does, that the goods were valueless. Except for diseased animals[143] and things like dangerous chemicals,[144] goods usually have some value even if only as scrap or salvage.[145] Nevertheless, the courts with regularity have upheld findings at the trial level based on the buyer's testimony that the delivered goods had no value. In such cases, the contract price is often found to be the measure of damages under section 2-714(2), the buyer having merely introduced evidence of that price as the value warranted and his own testimony that the goods were worthless.[146] It makes no difference that the buyer is merely a consumer and does not deal in the goods.[147]

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[138] *See* Special Project, *supra* note 30, at 115 (example of eggs held for over a month).

[139] Special Project, *supra* note 30, at 116.

[140] Courts have been willing to find resale price to be evidence of the value of the goods accepted. *See, e.g.*, ITT-Industrial Credit Co. v. Milo Concrete Co., Inc., 31 N.C. App. 450, 229 S.E.2d 814, 822 (1976)(resale price represents *some* evidence of value of goods at acceptance and is properly presented to jury); Bergenstock v. Lemay's G.M.C., 372 A.2d 69, 75 (R.I. 1977)(amount received at forced sale auction for truck is some evidence of truck's value at time of acceptance; inference that sale price approximated fair market value is not precluded by circumstance of forced sale). *But see* Alafoss v. Premium Corp. of Am., 599 F.2d 232, 237 (8th Cir. 1979)(court rejected price obtained upon resale because fair market value of goods at time of acceptance was higher); Judd Constr. Co. v. Bob Post, Inc., 33 Colo. App. 153, 516 P.2d 449, 451 (1973)(difference between purchase price of goods and allowance received on trade-in is not proper measure of damages for § 2-714 purposes).

[141] The buyer often uses expert testimony to prove value. *See, e.g.*, Soo Line R.R. Co. v. Freuhauf Corp., 547 F.2d 1365, 1377 (8th Cir. 1977)(vice president of railroad as expert); Carlson v. Rysavy, 262 N.W.2d 27, 32 (S.D. 1978)(expert on mobile home value); Melody Home Mfg. Co. v. Morrison, 502 S.W.2d 196, 202 (Tex. Civ. App. 1973)(mobile home dealer as expert).

[142] *See* Coyle Chevrolet Co. v. Carrier, 397 N.E.2d 1283, 1287 (Ind. Ct. App. 1980)(owner of personal property is competent to testify as to its value); Vreeman v. Davis, 348 N.W.2d 756, 757 (Minn. 1984)(owner is competent to express opinion on market value of his or her property and any weakness in foundation for that opinion goes to weight and not admissibility); Simmons v. C.W. Meyers Trading Post, Inc., 307 N.C. 122, 296 S.E.2d 294, 295 (1982)(error to exclude buyer's testimony on value of trailer without promised repairs); Williams v. Hyatt Chrysler-Plymouth, Inc., 48 N.C. App. 308, 269 S.E.2d 184, 190 (1980)(general rule is that non-expert witness who has knowledge of value gained from experience, information, and observation may give opinion of value of personal property); Chrysler-Plymouth City, Inc. v. Guerrero, 620 S.W.2d 700, 703 (Tex. Civ. App. 1981)(well settled rule is that owner of personal property can testify as to its

Often the case involves goods that would clearly seem to have some salvage value. For example, in *Peterson v. Bendix*

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value). *See also* Voytovich v. Bangor Puntar Operations, Inc., 494 F.2d 1208, 1210 (6th Cir. 1974)(court measured subjective value of defective boat according to buyer's intended use on particularly rough seas). *But see* KLPR TV, Inc. v. Visual Electronics Corp., 465 F.2d 1382, 1387-88 (8th Cir. 1972)(value to be considered is reasonable market value of goods delivered and not value of goods to particular purchaser or for particular purpose).

[143] *See, e.g.*, W & W Livestock Enter., Inc. v. Dennler, 179 N.W.2d 484, 490 (Iowa 1970)(court noted "dead pigs have no value").

[144] *See, e.g.*, Swenson v. Chevron Chemical Co., 234 N.W.2d 38, 44 (S.D. 1975)(farmer who paid $717 for defective pesticide entitled to recover that amount).

[145] *See* Michiana Mack, Inc. v. Allendale Rural Fire Protection Dist., 428 N.E.2d 1367, 1371 (Ind. Ct. App. 1981)(defective goods normally have at least scrap value); *see also Puritan Mfg. Co., Inc.*, 379 F. Supp. at 1314 (defendant could recover any salvage value); *Schatz Distrib. Co., Inc.*, 647 P.2d at 825 (measure of damages where computer found "worthless" is difference between zero and purchase price); *Raye*, 646 S.W.2d at 290 (measure of actual damages is difference in market value of produce as warranted and as delivered, exception exists when product is rendered valueless as result of defect and purchase price is then appropriate measure of actual damages); *Chrysler Corp.*, 618 S.W.2d at 805 (amount paid may be recovered if article has no value at all).

[146] *See, e.g.*, Peterson v. Bendix Home Sys., Inc., 318 N.W.2d 50, 56 (Minn. 1982)(upheld finding that mobile home had no value based on testimony of buyer); Simmons v. C.W. Myers Trading Post, Inc., 56 N.C. App. 549, 290 S.E.2d 710 (1982)(buyer who had lived in trailer competent to testify as to value).

[147] *See Peterson*, 318 N.W.2d at 56 (1982)(buyer of mobile home competent to testify to value); *Simmons*, 290 S.E.2d at 713 (buyer who lived in trailer competent to testify). *See also* AFA Corp. v. Phoenix Closures, Inc., 501 F. Supp. 224, 230 (N.D. Ill. 1980)(court accepted buyer's testimony that defects in part of shipment rendered total shipment valueless). *But see Puritan Mfg., Inc.* , 379 F. Supp. at 1314 (court, after upholding award to buyer of purchase price, suggested that "[i]n fairness, [the buyer] should tender liver and offal chillers to [the seller] which can then reclaim any salvage there might be in machinery.").

Home Systems, Inc., the seller argued on appeal that it was "particularly anomalous" for the buyer both to be awarded the full price of the mobile home in question and to be allowed to keep the home (in which he was apparently living).[148] The court's response to the seller's argument was rather pat. It merely said: "[The seller's] claim that [the buyer] gets a windfall by keeping the mobile home is negated by the jury's finding that the home has no value."[149] Of course, if the trier of fact does not believe the buyer's gratuitous testimony that the goods are worthless and the buyer has offered no additional evidence as to their value, the buyer will have failed to prove damages and may be denied any recovery under section 2-714(2).[150]

Unless the defect is sufficiently substantial to justify revocation of acceptance, section 2-714(2) requires that the value of the goods accepted be determined as of "the time and place of acceptance."[151] However, the permissible time frame for determining this value has varied from case to case, often depending on the nature of the goods. In *Tennessee-Carolina Transportation, Inc. v. Strick Corp.* the court suggested the following general rule:

> Where the value of personal property at a given point in time is an issue, evidence of its value within a reasonable time before or after such point is competent as bearing upon its value at the time in issue. Evidence of the property's value beyond a reasonable time before or after that point lacks probative force and is incompetent.[152]

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[148] *Peterson*, 318 N.W.2d at 55.

[149] *Id.* at 56.

[150] *See* Settell's, Inc. v. Pitney Bowes, Inc., 209 Neb. 26, 305 N.W.2d 896, 989 (1981)(buyer testified collator did not work but offered no evidence of value).

[151] U.C.C. § 2-608(1). Comment 3 to U.C.C. § 2-714 states: "If, however, the nonconformity is such as would justify revocation of acceptance, the time and place of acceptance under this section is determined as of the buyer's decision not to revoke." U.C.C. § 2-714 comment 3 (1978).

[152] Tennessee-Carolina Transp. Inc. v. Strick Corp., 286 N.C. 235, 210 S.E.2d 181, 184 (1974). *See also* KLPR TV, Inc. v. Visual Elec. Corp., 465 F.2d 1382, 1387 (8th Cir. 1972)(finding by trial court that leased television broadcasting equipment had no value was clearly erroneous where, inter alia, value was measured at time of trial nearly three years after delivery of equipment); Noreli Industries, Inc. v. Kleinert's, Inc., 57 A.D.2d 792, 394 N.Y.S.2d 687, 688 (1977)(no legal basis for valuation made months after delivery and acceptance).

The court then applied this rule to hold that the trade-in value some six years after the delivery and acceptance of certain defective trailers was too remote in time to be competent evidence of the value of the goods at the time of acceptance.[153]

4. A Case Synopsis: *Chatlos Systems, Inc. v. National Cash Register Corp*

The most informative judicial decisions to date on proving damages under the value differential formula in section 2-714(2) are the two decisions of the Third Circuit in *Chatlos Systems, Inc. v. National Register Corp.*[154] In *Chatlos* buyer purchased a computer system for approximately $40,000. The seller expressly warranted that the system would perform several specialized functions for the buyer. Although the computer system was apparently merchantable in that it was capable of performing a wide range of normal functions, it could not perform most of the warranted specialized functions required by the buyer. In particular, the computer could not process the buyer's inventory as warranted, and it apparently caused confusion within the buyer's record keeping. The payroll function did work for a time but then ceased. The seller's numerous attempts over an extended period of time to get the computer on line with respect to the various specialized functions were unsuccessful.[155]

After trial in the ensuing litigation, the buyer was awarded damages of approximately $120,000, of which approximately $57,000 represented value differential damages under section 2-714(2) and $63,000 represented consequential damages under

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But see Gray v. Davis, 45 Ill. App. 3d 55, 358 N.E.2d 1347, 1349 (1977)(award of damages upheld where seller failed to request instruction limiting testimony of fair market value of loader approximately two years after its delivery); *Coyle Chevrolet Co.*, 397 N.E.2d at 1288 (award of damages upheld based on buyer's opinion of defective car's value at time of trial where appellate court concluded that jury could have believed buyer's testimony pertained to value at time of acceptance, even though some defects were discovered later); *Vreeman*, 348 N.W.2d at 757-58 (seriousness of defects in manufacture of mobile home which only became evident over period of time constituted special circumstances permitting diminished value of mobile home to be ascertained at later date).

[153] *Tennessee-Carolina Transp.*, 210 S.E.2d at 184.

[154] 670 F.2d 1304 (3d Cir. 1982); 635 F.2d 1081 (3d Cir. 1980).

[155] *Chatlos*, 635 F.2d at 1083-84.

subsection (3).[156] On appeal, the court disagreed with the trial court's computation of damages and remanded the case for a redetermination. The appellate court first struck the buyer's recovery of consequential damages, finding that the contract of sale had validly excluded liability of the seller for such damages. This left the buyer with its $57,000 recovery for direct damages under subsection (2).[157]

However, the buyer argued that the trial court had erred in making this computation because it had excluded all evidence of market value of the goods and had simply held that the value as warranted was the contract price, including finance charges.[158] The trial court had reasoned that, because the term "market value" is conspicuously lacking from the text of subsection (2), the contract price was the best evidence of the value of the goods had they been as warranted. The trial court also included in its valuation the amount of some $5,600 that the buyer had paid for a service contract on the computer system. The court found the service contract to be inseparable from the remainder of the transaction.[159]

The Third Circuit agreed with the buyer's contention, holding that although in many cases fair market value and contract price will be identical, market price should always be the "starting point" for determining value under subsection (2).[160] The court reasoned that this would be the best way of protecting the bargain actually made so that a buyer would neither lose advantage of a good deal when the market for the goods has risen nor obtain unfair advantage when market value has declined. Thus, either party should always be entitled to show that market value and contract price are not identical. The court further held that the finance charges and cost of the service contract were not proper elements in determining the value of the goods. The court said that an award of such damages would constitute a windfall. The buyer would be able to make a cash replacement purchase for the goods without incurring such charges and to pocket the remainder.[161]

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[156] *Id.* at 1084.

[157] *Id.* at 1086-88.

[158] *Id.* at 1088.

[159] Chatlos Systems, Inc. v. National Cash Register, 479 F. Supp. 738, 744 (D.N.J. 1979).

[160] *Chatlos*, 635 F.2d at 1088.

The appellate court also questioned the trial court's computation of the value of the goods as accepted. The seller had warranted that the computer system would perform six specialized functions for the buyer, and the system was only able to perform one such function. The trial court thus concluded that the value of the system as accepted was one-sixth of the total contract price. The Third Circuit found this conclusion questionable because, although the buyer should be required to account for any benefit received from the goods, there was no evidence in the record demonstrating that each specialized function was to have the same value.[162]

On remand, the trial court determined that value differential damages under subsection (2) were approximately $202,000, and it entered judgment for the buyer in that amount plus prejudgment interest. The value of the computer as warranted was based primarily upon the testimony of the buyer's expert witness, who testified as to his estimate of the value of a computer system that would perform all of the specialized functions warranted by the seller. The seller countered with no expert testimony of its own, but merely contended the value as warranted was best represented by the contract price.[163]

On appeal, the Court of Appeals for the Third Circuit affirmed the judgment below. The court pointedly noted that the seller had waived its opportunity to submit independent evidence as to the value of the goods and had continued to maintain its contract price argument despite the court's previous holding on that point.[164]

The trial court had additionally found on remand that the value of the computer system as accepted was only approximately $6,000.[165] Over vigorous dissent by one judge, the Third Circuit upheld this valuation stating:

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[161] *Id.*

[162] *Id.*

[163] *Chatlos*, 670 F.2d at 1305-06.

[164] *Id.* at 1306.

[165] *Id.* at 1305 n.2.

> Although we might have come to a different conclusion on the value of the equipment as warranted had we been sitting as trial judges, we are not free to make our own credibility and factual findings. We may reverse the district court only if its factual determinations were clearly erroneous.[166]

There is also the moral of the benefits of vigorously litigating at trial the issues of valuation in computing general damages for breach of warranty under section 2-714.

5. The "Special Circumstances" Exception

Section 2-714(2) provides that the value differential formula is to apply in breach of warranty cases "unless special circumstances show proximate damages of a different amount."

The intent of the "special circumstances" exception is to allow the court to tailor damages to the facts and circumstances of the particular case so that the buyer is fully compensated for the injury suffered. Thus, what circumstances are "special" so as to come within the exception will vary from case to case. Special circumstances exist whenever an award for breach of warranty based upon the value differential provided in subsection (2), (including incidental and consequential damages), fails to place an aggrieved buyer in the position he would have occupied had the seller properly performed. A finding of such special circumstances takes the case out of subsection (2) and allows the court to fashion flexibly a damages award "in any manner which is reasonable" as provided by subsection (1). The goal of section 2-714 damages, regardless of how they are determined, is compensation and no more.

True "special circumstances" cases under section 2-714 are reasonably rare. It is quite uncommon to find cases which completely abandon the value differential formula in favor of a completely unrelated calculation. Usually the courts rely upon the exception merely to make slight adjustments in the value differential formula to fit the particular case. Very often the only modification made is to advance the time for fixing the value of the goods as accepted from the time of acceptance to some later time. The exception has also been relied upon to award repair[167] and replacement costs.[168]

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[166] *Id.* at 1307 (citing Krasnov v. Dinan, 465 F.2d 1298, 1302 (3d Cir. 1972)).

It is clear that the "special circumstances" exception sanctions lesser as well as greater damages than would be recovered under a strict application of the value differential formula.[169] For example, in *Simmons v. C.W. Myers Trading Post, Inc.*[170] the buyer's damages were pro-rated. The buyer leased a mobile home with an option to purchase. She agreed to pay $85 a month for ninety-six months, after which time she was to become the owner of the home. The home proved to be defective but was destroyed by fire after the buyer had lived in it for three years and had paid the seller a total of $2,370 on the purchase price.[171] The court found that these facts gave rise to "special circumstances" and that the buyer should be entitled to recover only a fraction of the difference between the fair market value of the home as delivered and the value of the home as warranted. The appropriate percentage was to be derived by taking the total payments made by the buyer divided by the total value of the home as warranted.[172]

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[167] See for example Mountaineer Contractors, Inc. v. Mountain State Mack, Inc., 268 S.E.2d 886 (W. Va. 1980) which involved the purchase of used bulldozers to be used in surface mining comparable industrial projects. The buyer accepted the bulldozers, despite certain defects, relying upon the seller's assurance that it would pay for all necessary repair expenses incurred by the buyer. *Id.* at 888-89. When the seller later refused to reimburse the buyer for these expenses, the buyer brought suit. The only instruction given to the jury on the issue of damages informed the jury that it could consider money spent by the buyer for parts and labor used in repairing the bulldozers and the loss of use of the bulldozers during the repair period. *Id.* at 889, 893. The appellate court affirmed a plaintiff's verdict stating that the method of assessing damages provided by the trial court was reasonable under the special circumstances of the case, namely, that the sale took place during a coal boom, at which time it was virtually impossible to purchase the type of bulldozers in question. The appellate court found that "in view of the economic situation of the industry at this time it would have been very difficult to ascertain the actual value of the equipment either at the time it was sold or at the time it was accepted . . ." *Id.* at 893. *See also* Vorthman v. Keith E. Meyers Enter. 296 N.W.2d 772 (Iowa 1980)(damages for diseased pigs warranted to be healthy were costs involved in curing disease).

[168] See City of New York v. Pullman, Inc., 662 F.2d 910 (2d Cir. 1981) *cert. denied*, 454 U.S. 1164 (1982) in which the City of New York sued for breach of warranty damages when subway cars it had purchased from Pullman had defective undercarriages. *Id.* at 912-13. The city argued that it came within the "special circumstances" provision of 2-714(2) because a subway car was a unique commodity not bought and sold in the market place, because of its concern for passenger safety, and because the design of the undercarriages was such that they could not be effectively repaired. The appellate court held that evidence of the current cost of replacing the defective undercarriages with undercarriages of a different design was properly admitted as relevant to the city's claim under the special circumstances provision. *Id.* at 918-20. *See also* Wright v. T & B Auto Sales, Inc., 325 S.E.2d 493, 496-97 (N.C. Ct. App. 1985)(special circumstances relied upon to award cost of new engine for used car where original engine completely destroyed as result of reversed engine heads).

[169] Vorthman v. Keith E. Meyers Enterprises, 296 N.W.2d 772, 777 (Iowa 1980).

[170] 56 N.C. App. 549, 290 S.E.2d (1982).

Similarly, in *Alafoss, H.F. v. Premium Corp. of America*[173] the court found that the buyer was overly compensated by an award of damages measured by the difference between the warranted value and the accepted value of non-conforming wrap coats purchased for resale. The facts indicated that a certain percentage of the coats would remain unsold in the buyer's mail-market program regardless of whether they had conformed to the seller's warranties. The court reasoned that the "special circumstances" exception mandated that this percentage be valued not in the retail market but in the bulk sale market where those coats would have been sold regardless of the seller's breach.[174]

Although no categorization of "special circumstances" cases can be exhaustive, at least six such categories are reflected by the reported decisions to date:

1. breach of warranty of title cases;
2. cases in which the court merely shifts the time for measuring value under the differential formula of subsection (2);
3. incidental and consequential damage cases;
4. diseased livestock cases where the entire herd is tainted although only a few of the animals are actually sick;
5. cases of crop loss resulting from defective herbicide;
6. cases where the buyer has mitigated damages to less than those provided by the value differential formula.

The first category of special circumstances cases, those involving a breach of warranty of title, deserve detailed attention and are discussed below.[175]

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[171] 290 S.E.2d at 711.

[172] *Id.* at 712-14.

[173] 599 F.2d 232 (8th Cir. 1979).

[174] *Id.* at 237-38.

[175] *See infra* notes 178-191 and accompanying text.

The second category of cases involves those in which the court measured value at other than the time and place of acceptance provided in subsection (2). The reasoning of the courts in these cases is supported by Comment 3 to section 2-714 which allows value to be measured at the time the buyer decides not to revoke acceptance in cases in which the defect would justify a revocation. The revocation situation can be viewed as simply a particularized example of a special circumstance which justifies a different time focus for measuring damages. In *Intervale Steel Corp. v. Borg & Beck Division, Borg-Warner Corp.*[176] for example, the buyer purchased steel coils from the seller on a regular basis for use in the fabrication of certain automobile components. The buyer's purchase order required that the coils meet strict specifications. Upon delivery of the coils, the buyer routinely began its fabrication process by stamping out "blanks" from the coils and storing them. About a month later, the buyer would resume its fabrication process. Cracking developed and the buyer discovered that the steel did not meet the agreed specifications. The seller admitted that the steel was non-conforming and authorized the buyer to scrap it.[177] At trial, the court awarded damages for breach of warranty under subsection (2) measured by the difference between the purchase price of the steel and its realized scrap value.[178] The seller argued that the scrap value did not provide any evidence of the actual value of the goods at the time and place of acceptance. The court acknowledged the seller's point, noted that subsection (2) does provide for value measurement at the time of acceptance and conceded that prior to its processing the steel had a variety of other uses and a value in excess of mere scrap.[179] Nevertheless, the court eschewed a "narrow reading" of section 2-714 and affirmed the trial court's judgment. The court said that a purely "objective calculation" of value would be inequitable to the buyer because the defect in the steel could not have been reasonably discovered until the steel was blanked out. The court reasoned that the "special circumstances" exception justified measuring the value of the steel at the time the defect was discovered.[180] The court said:

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[176] 578 F. Supp. 1081 (E.D. Mich. 1984).

[177] *Id.* at 1084-85.

[178] *Id.* at 1090.

[179] *Id.* at 1089.

> A logical interpretation suggests that the drafters intended 'special circumstances' to allow a shifting of the time-frame for assessing the perimeters of the 2-714(2) formula. Thus interpreted, the 'special circumstances' clause permits this court to look to some later point to determine the goods' value rather than the time of acceptance. Such 'special circumstances' exists in the instant case . . . .
>
> Therefore, the proper measure of damages pursuant to 2-714 is the difference between the price of the steel, representing 'the value . . . had [it] been as warranted,' and the scrap value of the steel after it had been blanked out into parts, which is the 'value of the goods accepted.'[181]

The courts have also used the "special circumstances" exception under subsection (2) to shift the time frame for measuring value so as to require the buyer to account for his use of the goods subsequent to acceptance, thereby reducing the damage award.[182] In this way, the buyer is compensated for his loss without being placed in a better position than he would have occupied had the goods been as warranted.

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[180] *Id.* at 1090-91.

[181] *Id.* For a case similarly decided, see Adam Metal Supply, Inc. v. Electrode, Inc., 386 So. 2d 1316 (Fla. Dist. Ct. App. 1980), wherein the buyer purchased aluminum sheeting which was discovered, after it had already been sheared, to be of a different kind than warranted. *Id.* at 1319. The court based damages on the value of the aluminum after it was sheared rather than its value at the time of acceptance. The court explained that:

> [T]he "special circumstances" of this case, namely the fact that it was necessary to shear the aluminum in order to determine that it was not Coilzak [as warranted], mandates that [the value of the aluminum accepted be ascertained after it was sheared] and makes it perfectly proper under section [2-714].

Id. at 1318.

See also Vreeman v. Davis, 348 N.W.2d 756 (Minn. 1984)(defects in mobile home were of such nature that their existence and seriousness only became evident over period of time and thus special circumstances permitted diminished value of goods to be ascertained at later date).

[182] *See, e.g.*, Ricklefts v. Clemens, 531 P.2d 94, 97 (Kan. 1975)(buyer of stolen automobile from innocent seller not entitled to full restitution since buyer had possession for nine months); Schneidt v. Absey Motors, Inc., 248 N.W.2d 792, 798 (N.D. 1976)(in action for breach of warranty of title to automobile, plaintiff not entitled to recover repair costs expended on automobile where expense did not flow from breach of warranty of title).

A third category of "special circumstances" cases includes those in which the court has utilized the exception to justify a buyers recovery of incidental and consequential damages. These cases represent an incorrect reading of section 2-714.[183] The "special circumstances" exception relates to direct damages in terms of the value differential in the goods as warranted and as accepted. Special damages, incidentals and consequential are a completely separate item of recovery and are provided for by subsection (3) rather than subsection (2). Although this error by the courts to date has been harmless, it does present the conceptual difficulty of allowing a buyer to recover special damages without meeting the specific requirements of section 2-715. This difficulty should be avoided.

A fourth category of "special circumstances" cases includes sales of diseased livestock as part of the sale of a herd under circumstances where it is difficult to determine precisely which animals are infected. For example, in *Holm v. Hansen*,[184] the buyer purchased a herd of cattle warranted by the seller to be healthy. Subsequent to acceptance, the buyer discovered that at least one of the cows was infected with brucellosis, a contagious disease. The buyer was unable to contain the disease, and it eventually spread through the herd.[185] The court on appeal held that it was error to limit the buyer's damages for loss of the herd to the difference between its value as warranted and its actual value at the time of purchase. The court said that the case came within the "special circumstances" exception of section 2-714. The court reasoned that, although some of the cattle that later became diseased were undoubtedly healthy at the time of acceptance, it was "neither realistic nor reasonable" for the trial court to limit the buyer's damages to conditions as they existed at that time. Nor should the buyer be penalized for retaining the cattle and caring for them in an effort to minimize his loss. The court thus concluded that fair and reasonable compensation to the buyer should include damages for the loss of the entire herd.[186]

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[183] For cases incorrectly identifying incidental and consequential damages under the "special circumstance" exception of subsection (2), see Lewis v. Mobile Oil Corp., 438 F.2d 500, 507, 510 (8th Cir. 1971)(loss of profits as consequential damages allowed under 2-714(2)); Murray v. Kleen Leen, Inc., 354 N.E.2d 415, 422 (Ill. App. Ct. 1976)(construction costs, less capital improvements awarded as consequential damages under 2-714(2)).

[184] 248 N.W.2d 503 (Iowa 1976).

[185] *Id.* at 505-06.

It has been suggested that results such as this need not be justified under the "special circumstances" exception. The argument is that goods with latent defects are no more valuable at acceptance than they will be when the defects surface. "The flock is a commercial unit only as healthy as its sickest contagious sheep."[187] Nevertheless, an occasional case would apparently limit the buyer's subsection (2) damages to the animals that were infected at the time of acceptance. Thus, in *Hepper v. Triple U Enterprises*,[188] the court denied the buyer any recovery because of an absence in the record of expert testimony to guide the jury in determining how many of the buffalo were infected at the time of purchase. The court said that without such information there was no way to discern reasonable damages under subsection (2).[189] The court's decision is unduly harsh unless the seller was able to show that the buyer acted unreasonably by allowing the remainder of the herd to become infected.

A fifth category of "special circumstances" cases involve crop losses resulting from defective herbicides or other agricultural chemicals. In these cases, the herbicide or chemicals contribute to a poor crop yield, and the courts typically award as damages the value the *crop* would have had if the herbicide or chemicals had conformed to the warranty less the value of the crop actually produced and less the expense saved by not preparing for market the portion of the probable crop which was prevented from maturing.[190] The following rationale from *Hill v.*

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[188] *Id.* at 510-11. It would seem, however, that some of the buyer's loss in this case was consequential since it is not likely that *all* of the cows were infected at the time of acceptance.

See also W & W Livestock Enter., Inc. v. Dennler, 179 N.W.2d 484 489 (Iowa 1970)(involved diseased pigs and court reached similar result without making reference to special circumstances exception); Hall v. Miller, 143 Vt. 135, 465 A.2d 222, 227-28 (1983)(diseased cattle).

[187] Special Project, *supra* note 30 at 126.

[188] 388 N.W.2d 525 (S.D. 1986).

[189] *Id.* at 530.

[190] *See, e.g.*, Simmons v. Ciba-Geigy Corp., 279 S.C. 26, 302 S.E.2d 17, 18 (1983)(sec-

BASF Wyandotte Corp. is typical:

> A herbicide failure is a latent defect in the product. There is no reasonable way a farmer can determine in advance whether a herbicide will perform as warranted. Discovery of the problem must await the development of the crop at which time it is usually too late to correct.
>
> The value of a herbicide as warranted is difficult to define. Price and value are not equivalents. From the farmer's perspective, the value of the herbicide is a healthy crop at maturity . . . .
>
> The value as accepted is equally uncertain and difficult to define. There is no market for such goods and thus no market price. If anything, it has a negative value.
>
> In our view, the inability of a court to ascertain with certainty the value of goods both as warranted and as accepted creates a special circumstance within the meaning of [section 2-714(2)]. It is this special circumstance which removes cases of this type from the [subsection (2)] measure of damages into subsection (1)."[191]

The *Hill* court's reasoning is obviously specious because the award was of consequential damages for the crop loss rather than direct damages for the purchased goods, the herbicide. Under subsection (2), the buyer's recovery should never exceed the warranted value of the goods, the fair market value of the herbicide at the time of acceptance. As is common in such sales, however, the seller excluded liability for consequential damages. Thus, cases like this are probably best understood as reflective of a public policy in farming states protecting farmers from catastrophic crop losses resulting from latent defects in farm products, such as herbicide and seed.

A sixth category of "special circumstances" cases is represented by those in which the buyer has mitigated his damages

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tion 2-714 not cited); Swenson v. Chevron Chem. Co., 234 N.W.2d 38, 44 (S.D. 1975).

[191] 311 S.E.2d 734, 736 (S.C. 1984). It should be noted that there was a valid limitation of consequential damages in this case. The court's response to the seller's argument that the formula employed by the court included lost profits was that: "[i]f the measure of damages we have adopted includes an element of lost profits, such inclusion is merely coincidental as the measure covers the direct loss resulting in the ordinary course of events from the alleged breach of the warranty." *Id.*

subsequent to acceptance of the defective goods so that his loss is actually less than the value differential at the time of acceptance. A good case on point is yet another involving the sale of diseased animals. In *Vorthman v. Keith E. Myers Enterprises*,[192] the seller wrongfully shipped diseased pigs with questionable market value to the buyer. The buyer nevertheless accepted the pigs and treated their disease. Through these efforts, the pigs were brought back to good health, and the buyer was able to resell them for the same price he would have expected had the pigs been healthy originally.[193] In measuring the buyer's damages under subsection (2), the court held that the "special circumstances" exception required that damages be limited to the fair value of healthy pigs for the fifty-five pigs which had died of the disease and the expenses the buyer had incurred in nursing the remainder of the herd back to health. The court reasoned that an award based on the true value differential of the pigs at the time of acceptance would over-compensate the buyer.[194] The case is an excellent example of the proposition that even direct damages are not recoverable if they can be reasonably avoided.

6. A Case Synopsis: *City of New York v. Pullman, Inc.*

A careful and helpful analysis of the "special circumstances" exception is provided by the second circuit opinion in *City of New York v. Pullman, Inc.*[195] The case fits into none of the categories discussed in the previous section above and thus well demonstrates that special circumstances under section 2-714 will ultimately be determined by the facts of the individual case.

Pullman agreed to sell subway cars to the New York City Transit Authority for a price of $210 million. Pullman subcontracted the undercarriages for the cars to Rockwell for a price of approximately $20 million. The undercarriages were radically different from any that had been used on subway cars previously in the city of New York. Once put into use, the undercarriages caused the subway cars to vibrate excessively and to crack, thereby giving rise to safety problems. Pullman and Rockwell designed a system, called "retrofit," to repair the cars. However, they declined the City's request that they conduct additional tests to determine the actual effect the retrofit would have on the cars. Experts hired by New York concluded that the retrofit would not solve the vibration, cracking and safety problems.[196]

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[192] 296 N.W.2d 772 (Iowa 1980).

[193] *Id.* at 774.

[194] *Id.* at 778. The plaintiff had, in essence, "repaired" the pigs and was therefore entitled to his cost of repair.

[195] 662 F.2d 910 (2d Cir. 1981), *cert. denied*, 454 U.S. 1164 (1982).

At trial, New York claimed damages in the amount of $98 million measured by the cost of replacing the undercarriages with standard ones.[197] Pullman and Rockwell submitted that the replacement with standard undercarriages would cost only $48 million. They further claimed that the accurate measure of damages was the cost of the retrofit which they estimated at $36 million. The trial court instructed the jury that the measure of damages was the value differential provided in section 2-714(2) unless the buyer came within the special circumstances exception. The court further instructed that the jury could find that the following facts, taken together, constituted such special circumstances: (1) that a subway car is a unique commodity not bought and sold in the market place; (2) the proper and necessary concern by the buyer for passenger safety; and (3) that the unique design of the undercarriages rendered them incapable of effective repair.[198] The jury returned a general verdict for New York in the amount of $72 million.[199]

On appeal, the Second Circuit affirmed the judgment opining that the recovery was justified even without a finding of special circumstances.[200] The court reasoned that the cost of replacement with standard undercarriages was good evidence of the value differential at the time of acceptance between the value warranted, safe subway cars, and the value accepted, unsafe cars.[201] The court's conclusion in this regard, however, is a bit tenuous because the repairs with standard undercarriages would not bring the cars into conformance with the contract description for the goods.[202]

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[196] *Id.* at 912-13.

[197] *Id.* at 915-16. New York also claimed consequential damages for the cost of the inspection and spot-welding program conducted on the defective subway cars under the terms of the contract. *Id.* The trial court declined to instruct the jury on this claim, stating that it would give only "a simplified charge" to the jury. *Id.* at 917 n.8. Surprisingly, the Second Circuit upheld this decision. *Id.* The trial court's procedure would seem to be in direct contravention of § 2-714(3).

[198] *Id.* at 916.

[199] *Id.* at 912.

[200] *Id.* at 912, 920.

The court then rejected the seller's claim that the trial court erred in permitting the jury to assess damages under the "special circumstances" exception. The court said that there was ample evidence from which the jury could have found that the value differential formula would not have compensated the buyer. The court emphasized the lack of available alternatives on the open market and the necessary safety concerns of the buyer for its passengers. These special circumstances justified a recovery determined in any manner that was reasonable.[203] The court said:

> An appropriate measure of damages under [the special circumstances] provision is the 'actual cost' of a remedy that meets the ultimate requirements of the contract by converting nonconforming goods into goods which will perform as warranted —even if that remedy requires replacing defective parts with parts substantially different than those provided under the contract, at a time later than delivery — as long as that remedy meets the ultimate requirements of the contract . . . .[204]

The court thus rejected the further contention of the seller that current replacement costs of the defective undercarriages was irrelevant. Under the "special circumstances" exception, repair costs could be determined on the basis of the costs at the time of trial.[205]

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[201] *Id.* at 915-17.

[202] *Id.* The court also rejected appellants' argument that the trial court erroneously failed to instruct the jury as to a third measure of repair costs (repair with recase undercarriages). *Id.* The court found no probative evidence in the trial record that this method was a viable means of repair. *Id.* at 917.

[203] *Id.* at 917-18.

[204] *Id.* at 918.

[205] *Id.*

7. Breach of Warranty of Title

Under the Uniform Sales Act, damages for breaches of warranty of title and warranty of quality were usually treated separately.[206] Although some commentators have suggested that this separate treatment continues under the Uniform Commercial Code,[207] section 2-714 makes no such distinction and the courts have applied none.[208] However, the general formula in section 2-714(2) is poorly suited for computing damages in most warranty of title cases, and thus damages must usually be calculated under the "special circumstances" exception.[209]

In a typical breach of warranty of title case, *Murdock v. Godwin,*[210] the buyer unwittingly purchased a stolen car. After receiving a certificate warranting title to the car to be free from all liens and encumbrances, the buyer made use of the vehicle for a period of time before it was seized by law enforcement officers.[211] The buyer then brought an action against the seller for breach of warranty of title under section 2-312.[212] The *Murdock*

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[206] *See* Uniform Sales Act § 69(6) & (7). *See generally* Metalcraft, Inc. v. Pratt, 500 A.2d 329, 335-36 (Md. Ct. Spec. App. 1985)(discussing courts and commentators who made such distinctions); Menzel v. List, 24, N.Y.2d 91, 96, 298 N.Y.S.2d 979, 982, 246 N.E.2d 742 (1969)(same).

[207] *See* R. Anderson, Uniform Commercial Code § 2-714:26 (3d ed. 1983); A. Squillante & J. Fonseca, Williston on Sales § 16-8 (2)(4th ed., 1974).

[208] *See* W. Hawkland, Uniform Commercial Code Series § 2-714:03 (1982); *see also* Jeanneret v. Vichey, 541 F. Supp. 80-85 (S.D.N.Y. 1972)(equating warranties of title and quality), *rev'd*, 693 F.2d 259, 267-68 (2d Cir. 1982); City Car Sales, Inc. v. McAlpin, 380 So. 2d 865, 868-69 (Ala. Ct. App. 1979)(same), *cert. denied*, 380 So. 2d 869 (Ala. 1980); Ricklefts v. Clemens, 531 P.2d 94, 100-01 (Kan. 1975)(same); Itoh v. Kimi Sales, Ltd., 345 N.Y.S.2d 416, 420 (N.Y. Civ. Ct. 1973)(same), *rev'd*, 494 N.Y.S.2d 598 (1985); Schneidt v. Absey Motors, Inc., 248 N.W.2d 792, 797-8 (N.D. 1976)(same).

[209] For an excellent judicial analysis of measuring damages in breach of warranty of title cases, see *Metalcraft*, 500 A.2d at 329.

[210] 269 S.E.2d 905 (Ga. Ct. App. 1980).

[211] *Id.* at 907.

[212] Section 2-312 of the Uniform Commercial Code provides:

> (1) Subject to subsection (2) there is in a contract for sale a warranty by the seller that:
>
> (a) the title conveyed shall be good, and its transfer rightful; and
>
> (b) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.
>
> (2) A warranty under subsection (1) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that

court determined that the financed purchase price represented the value of the automobile as warranted and that the value as accepted was zero.[213] The seller argued on appeal that the recovery should have been reduced to take into account the buyer's uninterrupted use of the automobile for nearly three years prior to its being seized. The court on appeal rejected this argument, holding that "the trial court was correct in excluding irrelevant evidence as to the value of [the buyer's] use of the automobile subsequent to" the time of acceptance.[214] Quite clearly, the buyer in this case received a windfall.

In factually similar cases, most courts have relied on the "special circumstances" exception in subsection (2) and have awarded damages measured by the value of the item when it was taken from the buyer. Application of this measure of damages usually places the buyer in the position he would have occupied had the seller supplied good title. As a New York court explained:

> A case involving breach of warranty of title, where stolen property is taken away from the buyer at some time after the purchase, is one where there are special circumstances so that the measure of damages should be the value of such property when it is taken away. In this way, the buyer will receive what he has 'actually lost.' He will get the benefit of any appreciation in value . . ., including items of value he may have added to the stolen property . . .; and, on the other hand, he will not be unduly enriched by depreciation in the value of the property, from the use of which he benefitted until it was taken from him . . . ."[215]

> the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.
>
> (3) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.

U.C.C. § 2-312 (1978).

[213] *Murdock*, 269 S.E.2d at 908.

[214] *Id.* at 907. This appears to be the only case which has strictly applied the value differential formula in § 2-714 (2) without taking into consideration the special circumstances of a breach of warranty of title case.

[215] Itoh v. Kimi Sales, Ltd., 345 N.Y.S.2d 416, 420 (N.Y. Civ. Ct. 1973). *See also*

It is not uncommon in warranty of title cases for the buyer to have been deprived of effective use of the goods before he relinquished actual possession of them. Thus, in one case the buyer purchased an automobile and received a certificate of title warranting it to be free from all liens and encumbrances except as specified. He drove the automobile for approximately nine months until he was notified by an agent of the Federal Bureau of Investigation that the automobile was stolen and that the buyer risked being arrested if he were to continue driving it. The buyer discontinued operating the vehicle but continued possession for another nineteen months, at which time judgment in replevin was entered against him in favor of the vehicle's true owner. In his suit against the seller for breach of warranty of title, the buyer was awarded the value of the automobile on the date the order of replevy was entered.[216] On appeal, the court reversed and remanded the case with instructions that the buyer should be awarded as damages the value of the automobile on the date he was notified by the F.B.I. agent to discontinue its use.[217] Other courts are in general agreement with this decision and hold that, when a buyer loses the effective use of an item prior to the date he is deprived of actual possession, the former date is the correct time for calculating the value of the goods.[218]

Purchase price, of course, is not necessarily the proper measure of value in a breach of warranty of title case any more than it is in other section 2-714 case. Nevertheless, purchase price is admissible as evidence of value unless the evidence demonstrates that the amount will overcompensate or undercompensate the aggrieved buyer.[219] For example, the buyer may receive

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DeWeber v. Bob Rice Ford, Inc., 590 P.2d 103, 104-05, (Idaho 1979)(stolen automobile which passed through numerous hands before fact of theft was discovered resulted in lawsuits up purchase chain).

[216] Ricklefts v. Clemens, 531 P.2d 94 (Kan. 1975).

[217] *Id.* at 101.

[218] *See* City Car Sales v. McAlpin, 380 So. 2d 865, 868 (Ala. Ct. App. 1979), *cert. denied* 380 So.2d 869 (Ala. 1980)(correct measure of damages for breach of warranty of title is value of vehicle at time buyer effectively loses use of it); *accord* Schneidt v. Absey Motors, Inc., 248 N.W.2d 792, 798 (N.D. 1976). *See generally* Annotation, *Measure of Damages in Action for Breach of Warranty of Title to Personal Property Under UCC Section 2-714*, 94 A.L.R.3d 585 (1979).

[219] *Riclefts*, 531 P.2d at 100. *See also Schneidt*, 248 N.W.2d at 798; Itoh v. Kimi

a windfall in cases in which he has had uninterrupted use of the item for some period of time prior to its being taken from him unless the fair value of that use is offset against the purchase price. Conversely, the buyer will be undercompensated by a valuation based on the purchase price if the goods have appreciated in value or if the buyer otherwise had struck a particularly good bargain.[220] Thus, in one case the buyer innocently purchased a stolen oil painting for $4,000.[221] At the time the buyer was forced to relinquish the painting to its true owner it was worth $22,500. On appeal, the court held that the correct measure of damages was the value of the painting when the buyer surrendered it.[222] The court thereby attempted to place the buyer in the position he would have occupied had title been as warranted. Unfortunately, in situations where the goods continue to appreciate compensation goals sometimes cannot be fully attained by measuring damages at any particular point in time.

Not all breach of warranty of title cases involve stolen goods which the buyer has been required to relinquish. Often the breach under section 2-312 is simply one of "quiet enjoyment" of the goods where an undisclosed lien or other encumbrance clouds the title. The damages in such cases are usually measured by the cost of removing the lien or encumbrance.[223]

Sales, Ltd., 345 N.Y.S.2d 416, 419 (1973); *overruled on other grounds*. 494 N.Y.S.2d 598 (1985); Miles v. Lyons, 6 U.C.C. Rep. Serv. (Callaghan) 659 (Mass. Dist. Ct. 1969); *City Car Sales*, 380 So. 2d at 868. *But see* John St. Auto Wrecking v. Motors Inc., 288 N.Y.S.2d 281, 284-85 (1968)(purchase price paid regarded as proper item of damage).

[220] *See supra* notes 112-132 and accompanying text.

[221] Menzel v. List, 24 N.Y.2d 91, 246 N.E.2d 742, 298 N.Y.S.2d 979 (1969).

[222] Menzel v. List, 24 N.Y.2d at 98, 246 N.E.2d at 746, 298 N.Y.S.2d. at 984. *See* Jeanneret v. Vichey, 541 F. Supp. 80, 85 (S.D.N.Y. 1982)(buyer entitled to appreciated value of painting in action for breach of warranty of title); *Miles*, 6 U.C.C. Rep. Serv. (Callaghan)at 66, (breach of warranty of title damages of $275 awarded for furniture purchased for $100 on ground that buyers were entitled to benefit of bargain); *see also Metalcraft*, 500 A.2d at 42, in which the court states:

> [section] 2-714(2) speaks of 'special circumstances [that] show proximate damages of a *different* amount.' 'Different' may be either greater or less, and we hold that the proper measure of damages is indeed the value of the goods at date of dispossession whether that value be larger or smaller than the value of the goods at acceptance.

[223] *Id. See, e.g.*, Catlin Aviation Co. v. Equilease Corp., 626 P.2d 857, 861 (Okla. 1981).

8. Incidental and Consequential Damages — Section 2-714(3)

General (direct) damages recoverable under subsections (1) and (2) of section 2-714 will frequently be insufficient to make the buyer whole without an additional allowance for incidental and consequential damages resulting from the seller's breach.[224] Subsection (3), therefore, expressly authorizes the recovery of these special (indirect) damages "in a proper case." A "proper case" is one which meets the requirements expressly set forth in section 2-715 for the recovery of incidental and consequential damages.[225]

The distinction between incidental and consequential damages is often not an easy one to make.[226] Fortunately, with respect to claims by buyers, the distinction is not often important unless the seller has excluded liability for the one (usually consequential) but not the other.[227] For purposes of simplicity, incidental and consequential damages will be jointly referred to in this section as "special damages."[228]

Particularly in early cases construing section 2-714, a number of courts have confused special damages under section 2-715 with the "proximate damages of a different amount" referred to in the "special circumstances" clause of section 2-714(2).[229] How this confusion could arise is quite understandable. The "special circumstances" language in subsection (2) is identical to that used by Baron Alderson in the great case of *Hadley v. Baxendale*[230] to describe consequential damages. The choice of language in subsection (2) is thus perhaps unfortunate because, when a contracts lawyer or a judge hears the phrase "special circumstances" in reference to contract damages, the immediate thought is of consequential loss. To further the confusion, general damages are described differently in subsections (1) and (2) but subsection (2) is clearly a subset for measuring damages under subsection (1). Thus, it is not illogical to interpret a "proper case" under subsection (3) to be merely a subset of the "special circumstances" clause in subsection (2).

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[224] *See* U.C.C. § 2-714 comment 4 (1978)(incidental and consequential damages usually accompany action brought under § 2-714).

[225] Section 2-714 of the Uniform Commercial Code provides:

> (1) Incidental damages resulting from the seller's breach includes expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.
>
> (2) Consequential damages resulting from the seller's breach include
>
> > (a) any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and
> >
> > (b) injury to person or property proximately resulting from any breach of warranty.

Id.

[226] For a detailed discussion of the distinction, see Anderson, *A Roadmap for Sellers' Damages Remedies Under the Uniform Commercial Code and Some Thoughts About Pleading and Proving Special Damages*, 19 Rutgers L.J. 245, 269-73 (1988); Anderson, Incidental and Consequential Damages, 7 The J. of L. and Con. 327, 333-39 (1987)[hereinafter *Incidental and Consequential Damages*]. *See generally* R. Anderson, Damages Under the Uniform Commercial Code §§ 2:14 and 11:03 (1988)[hereinafter Damages].

[227] *See supra* notes 1-22 and accompanying text.

[228] *See generally* Special Project, *supra* note 30, at 140-43.

Although thus quite understandable, the error should be avoided. A recovery under subsection (3) is not governed by the other provisions of section 2-714 but is subject to section 2-715. While most courts today are clear on the point, an occasional case overlooks it, with the result that lump sum damages are awarded without identifying the general and special damages.[231] The court then, by assuming that the entire award is of general damages under section 2-714(1), inadvertently allows the buyer a recovery for special damages without having met the particular requirements (foreseeability, avoidable loss, etc.) provided in section 2-715.[232] Further, in cases in which the contract goods would be consumed by the buyer in the process of making a profit, a recovery which lumps general and consequential damages allows the buyer a windfall. For example, in a typical case the seller sells defective feed to a buyer in the business of raising and selling livestock. If the bad feed decimates the herd, the buyer may certainly recover consequential damages for lost profits that would have been earned from selling the herd if the buyer can meet the requirements of foreseeability, certainty and unavoidability provided in section 2-715.[233] The loss is clearly consequential under section 2-715(2)(a). However, the buyer should not be allowed additionally to recover general damages under section 2-714 based on the warranted value of the feed because that feed would have been consumed in the process of preparing the animals for market and in earning the profits from their sale. Had the contract been performed, the buyer would not have been in the position of both having the feed as warranted and the profit that would have been earned.[234]

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[229] *See* Lewis v. Mobile Oil Corp., 438 F.2d 500, 507-08 (8th Cir. 1971)(using § 2-715 to measure damages in "special circumstances" case); Prutch v. Ford Motor Co., 574 P.2d 102, 104 (Colo. 1980)(same), *rev'd*, 618 P.2d 657 (*en banc*); Lanphier Constr. Co. v. Fowco Constr. Co., 523 S.W.2d 29, 41-42 (Tex. Civ. App. 1975)(same); General Supply & Equip. Co. v. Phillips, 490 S.W.2d 913, 919 (Tex. Civ. App. 1972)(same).

[230] 156 Eng. Rep. 145 (1854). The case is usually credited with establishing in the law of contracts allowance for the recovery of special damages. *See* G. GILMORE, THE DEATH OF CONTRACT, 49-53, 83 (1974)(describing Hadley v. Baxendale as "a fixed star in the jurisprudential firmament" and stating : "since 1854 the starting point for all discussion of contract damage theory has been Hadley v. Baxendale"). *See generally* Danzig, *Hadley v. Baxendale: A Study in the Industrialization of the Law*, 4 J. LEGAL STUD. 249 (1975)(tracing interrelated evolutions in economics and contract damage theory).

[231] J. WHITE & R. SUMMERS, *supra* note 4, at 386 n.48 (citing Baden v. Curtis Breeding Service, 380 F. Supp. 243 (D. Mont. 1974)); Russo v. Hilltop Lincoln-Mercury, Inc., 479 S.W.2d 211 (Mo. Ct. App. 1972).

Similarly, in a case involving the sale of insecticide, the court erred by allowing the buyer a duplicate recovery.[235] The buyer sued the manufacturer for damage to his corn crop resulting from the failure of the insecticide to work properly. The court found that the insecticide was without value as accepted and awarded the full $717 purchase price as value differential damages under section 2-714(2). Additionally, the court awarded the difference between what the buyer's crop would have been worth at maturity and its actual worth at maturity, less any savings in labor and expenses attributable to the reduced yield.[236]

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[232] The matter is discussed in *Incidental and Consequential Damages*, *supra* note 226, at 328-33. *See also* DAMAGES, *supra* note 226, at § 11:01.

[233] See § 1-106 of the U.C.C. and the Official Comment thereto for a discussion of "certainty".

[234] For a case in which the court erred by allowing such a double recovery, see R.E.B., Inc. v. Ralston Purina Co., 525 F.2d 749, 753-59 (10th Cir. 1975).

[235] Swenson v. Chevron Chemical Co., 234 N.W.2d 34 (S.D. 1975).

[236] *Swenson*, 234 N.W.2d at 43-44. *See also* R. Clinton Construction Co. v. Bryant & Reaves, Inc., 442 F. Supp. 838, 846 (N.D. Miss. 1977)(purchase price of defective antifreeze recovered in addition to "reasonable cost of the labor and parts necessary to repair the damaged machinery and of loss of income to [buyer] during the down-time occasioned by the period of repairs").

Evidently, this additional award was for consequential damages under section 2-715. However, since the insecticide would have been consumed in producing an undamaged matured crop, the buyer received a $717 windfall under the court's calculation of damages.

The buyer may also receive an unfair windfall if the court lumps general and special damages under section 2-714(2) in a case in which the seller has properly excluded liability for special damages. Most cases which make this error involve crop losses resulting from defective feed, herbicide or fertilizer, and one suspects that such decisions merely reflect an unspoken judicial or public policy in agricultural states favoring protection for farmers from potentially catastrophic consequential losses.[237] Even so, it would be more appropriate and less confusing for the court to attack the seller's consequential damage excluder directly under the applicable Code provisions in section 2-719.[238]

III. LITIGATION ASPECTS OF DAMAGES FOR ACCEPTED GOODS

A. *Burden of Proof*

The buyer has the burden of proving any breach with respect to accepted goods,[239] including the burden of establishing damages.[240] However, the damages do not have to be proved with mathematical precision.[241] The buyer need only establish a reasonable basis for ascertaining damages.[242]

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[237] *See, e.g.*, Hill v. BASF Wyandotte Corp., 311 S.E.2d 734 (S.C. 1984)(defective herbicide case in which buyer awarded difference between value crop would have had if herbicide had been as warranted and value crop actually had, less expenses of preparing for market portion of crop lost despite valid limitation on special damages).

[238] *See, e.g.*, Trinkle v. Schumacher Co., 301 N.W.2d 255, 258-59 (Wisc. Ct. App. 1980)(limitation of damages clause in sales contract disallowing any claims after cutting of fabric held unconscionable under § 2-719(3) where defect not discovered until cutting).

[239] U.C.C. § 2-607 (4)(1978).

[240] *See* KLPR TV, Inc. v. Visual Elec. Corp., 327 F. Supp. 315, 327-28 (W.D. Ark., 1971)(placing burden to prove all elements of claim on plaintiff); Bob Anderson Pontiac, Inc. v. Davidson, 293 N.E.2d 232, 237 (Ind. Ct. App. 1973)(same); Stair v. Gaylord, 659 P.2d 178 (Kan. 1983)(same); State *ex rel.* Hawkins-Hawkins Co. v. Travelers Indemnity Co., 442 P.2d 612, 613 (Or. 1968)(same).

[241] U.C.C. § 1-106, comment 1 (1978).

[242] Central Bit Supply, Inc. v. Waldrop Drilling & Pump, Inc., 717 P.2d 35 (Nev.

Under the value differential formula of subsection (2), the burden is on the buyer to show that differential at the time and place of acceptance.[243] Where no evidence is submitted as to the value of non-conforming goods at the time and place of acceptance, nor any other evidence from which to determine the value differential, the buyer is properly held to have failed to carry his burden of proof.[244] The burden of proof is not difficult to carry but some courts are more permissive than others. It is not uncommon, particularly in consumer cases, for damages to be awarded based on repair costs when that is the only evidence in the record from which to calculate damages.[245]

Occasionally the courts have intervened to save a buyer's attorney who failed to properly present evidence of damages. In one case, when the buyer offered no appropriate evidence as to value, "official notice" was taken of federal market quotations for the applicable time and place.[246] In a rather extraordinary case, the court awarded damages based exclusively on a statement in the complaint when no evidence was presented at trial to disprove the buyer's allegations.[247] One is, of course, never safe in assuming that such a permissive attitude will be demon-

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1986); *Bob Anderson Pontiac*, 293 N.E.2d at 237.

[243] Uganski v. Little Giant Crane & Shovel, 192 N.W.2d 580, 592 (Mich. Ct. App. 1971)(burden of proving difference in value on purchaser); Williams v. Hyatt Chrysler-Plymouth, Inc., 269 S.E.2d 184, 189 (N.C. Ct. App. 1980)(same); Stutts v. Green Ford, Inc., 267 S.E.2d 919, 926 (N.C. Ct. App. 1980)(same); HPS, Inc. v. All Wood Turning Corp., 204 S.E.2d 188, 190-91 (N.C. Ct. App. 1974)(same); Newman v. Spector Wrecking & Salvage Co., 490 S.W.2d 875, 877 (Tex. Civ. App. 1973)(same).

[244] Atlan Indus. Inc. v. O.E.M., Inc., 555 F. Supp. 184, 189 (W.D. Okla. 1983). *See also* Fargo Mach. & Tool Co. v. Kearney & Trecker Corp., 428 F. Supp. 364, 382-83 (E.D. Mich. 1977)(buyer failed to offer adequate evidence of expenditures for repairs or any other evidence against which to calculate damages for breach of warranty); Settell's, Inc. v. Pitney Bowes, Inc., 305 N.W.2d 896, 899 (Neb. 1981)(buyer failed to carry burden of proof as to damages even though subsection (2) allows alternative rules for proving damages in any manner that is reasonable, such as costs of repair or market value as quoted in official sources).

[245] *See, e.g.*, Bendix Home Sys., Inc., v. Jessop, 644 P.2d 843, 847 (Alaska 1982)(absent evidence of value of mobile home at issue, court awarded repair costs); Mileham & King. Inc. v. Fitzgerald, 33 U.C.C. Rep. Serv. (Callaghan) 208, 216 (D.C. 1982)(cost to repair shutters awarded where no other evidence of damages was submitted).

[246] Jerome Kantro Co. v. Summers Bros., Inc., 27 Agric. Dec. 129, 135-37 (U.S. Dept. Agric. 1968).

[247] McNair Constr. Co. v. Fogle Bros. Co., 307 S.E.2d 200, 204 (N.C. Ct. App. 1968).

strated by a particular court.

B. *Sufficiency of Evidence*

While damages must be proved with reasonable certainty and may not be based on mere speculation, mathematical certainty is not required. Evidence of damages is sufficient if it is the best evidence available and if it affords a reasonable basis for estimating the loss.[248] The courts have commonly accepted the purchase price as prima facie evidence of the value of the goods as warranted,[249] and the amount at which the defective goods were resold has been held to constitute some evidence of the value of the goods as accepted if the resale was commercially reasonable and not unduly delayed.[250] Since proving the value of the goods as accepted is often quite difficult, the courts liberally accept cost of repairs as adequate evidence of the value differential between the goods as warranted and as accepted.[251]

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[248] *See* Great West Food Packers v. Longmont Foods Co., 636 P.2d 1331, 1333 (Colo. Ct. App. 1981)(holding that speculative damages should only be disallowed where fact of damages is uncertain, not where amount is uncertain); Lovington Cattle Feeders v. Abbott Laboratories, 642 P.2d 167, 171-72 (N.M. 1982)(same); Barnard v. Compugraphic Corp., 667 P.2d 117, 120 (Wash. Ct. App. 1983)(same).

For cases holding the buyer's evidence sufficient to prove damages, see Teledyne Indus. v. Patron Aviation, Inc., 288 S.E.2d 911, 912-13 (Ga. Ct. App. 1982); Willmar Cookie Co. v. Pippin Pecan Co., 357 N.W.2d 111, 114 (Minn. Ct. App. 1984); Peterson v. North Am. Plant Breeders, 354 N.W.2d 625, 633-34 (Neb. 1984); Vista St. Clair, Inc. v. Landry's Commercial Furnishings, Inc., 643 P.2d 1378, 1381-82 (Or. Ct. App. 1982).

For cases in which the buyer's evidence was held insufficient to prove damages, see Overseas Motors Corp. v. First Century Christian Church, Inc., 608 S.W.2d 288, 289-90 (Tex. Civ. App. 1980); Fredrick v. Dreyer, 257 N.W.2d 835, 840 (S.D. 1977).

[249] *See* Thompson Chrysler Plymouth, Inc. v. Myers, 264 So. 2d 893, 897, (Ala. Civ. App. 1972)(cost is admissible on issue of valuation, unless too remote); W & W Livestock Enter. v. Kennler, 179 N.W.2d 484, 489-90 (Iowa 1970)(same); Auto-Teria, Inc. v. Ahern, 352 N.W.2d 774, 783 (Ind. Ct. App. 1976)(same); Lyon v. Shelter Resources Corp., 253 S.E.2d 277, 281 (N.C. Ct. App. 1979)(same); K & C, Inc. v. Westinghouse Elec. Corp., 263 A.2d 390, (Pa. 1970)(same).

[250] *See* Lackawanna Leather Co. v. Martin & Steart, Ltd., 730 F.2d 1197, 1203 (8th Cir. 1984)(stating that resale value is adequate indication of value of goods as received); ITT-Industrial Credit Co. v. Milo Concrete Co., 229 S.E.2d 814, 822 (N.C. Ct. App. 1976)(same); *see also* Uganski v. Little Giant Crane & Shovel, Inc., 192 N.W.2d 580, 592 (Mich. Ct. App. 1971)(where resale had been unreasonably delayed, court held that plaintiff had burden to prove that resale price was fair market value); Tennessee Carolina Transp. v. Strick Corp., 210 S.E.2d 181, 184 (N.C. 1974)(same). *But see* S.C. Gray, Inc. v. Ford Motor Co., 286 N.W.2d 34, 41 (Mich. Ct. App. 1979)(evidence limited to purchase price and salvage value held insufficient to support damage award absent additional evidence regarding actual value of goods).

An owner is competent to testify as to his opinion of the value of the goods, and any weakness in the foundation of that opinion goes to its weight and not to its admissibility.[252] However, recovery will be denied for any sentimental or otherwise subjective value which the owner might place on his property.[253]

C. *Mitigation of Damages*

The common law damage doctrine of avoidable consequences permeates all damage remedies under the Code. One is not allowed to recover damages that could have been reasonably avoided, and this includes damages arising from accepted goods.[254] In accepted goods cases issues regarding, the buyer's failure to mitigate usually arise with respect to incidental or consequential damages.[255] A failure to act reasonably to mitigate damages will result in the buyer's damage award being reduced by any damages that could have thereby been avoided.[256] The only requirement, however, is that the buyer act reasonably, and there is no need for resort to extraordinary measures.[257] However, the buyer may be called upon to spend money to mitigate damages where the amounts are small in comparison to the potential loss and where the risks involved are not great.[258] It has been held that a seller may not insist upon mitigation of damages if he has led the buyer to believe that he will repair the goods in time to avoid further loss.[259]

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[251] *See* Winchester v. McCulloch Bros. Garage, 388 So. 2d 927, 928-29 (Ala. 1980)(basing recovery on repair cost); *see also* In re Precise Tool & Gauge Co., 42 Bankr. 677, 680-81 (E.D. Tenn. 1984)(same); Hahn v. Ford Motor Co., 434 N.E.2d 943, 955 (Ind. Ct. App. 1982)(same); S.H. Nevers Corp. v. Husky Hydraulics, Inc., 408 A.2d 676, 681 (Me. 1979)(same); Foremost Mobile Homes Mfg. Corp. v. Steele, 506 S.W.2d 646, 649 (Tex. Civ. App. 1974)(same).

[252] *See* Ricker v. Hopkins Chevrolet, Inc., 248 S.E.2d 720, 722 (Ga. Ct. App. 1978)(to testify as to value one need only to have had opportunity to form correct opinion); Tarter v. MonArk Boat Co., 430 F. Supp. 1290, 1294 (E.D. Mo. 1977)(same); Griese v. Cory Pools, Ltd., 373 N.E.2d 1383, 1385 (Ill. Ct. App. 1978)(same); Coyle Chevrolet Co. v. Carrier, 397 N.W.2d 1283, 1287 (Ind. Ct. App. 1979)(same); Vreeman v. Davis, 348 N.W.2d 756, 757-58 (Minn. 1984)(same); Simmons v. C.W. Myers Trading Post, Inc., 290 S.E.2d 710, 713 (N.C. 1982)(same); Chrysler-Plymouth City, Inc. v. Guerrero, 620 S.W.2d 700, 703-4 (Tex. Civ. App. 1981)(same); Wharton Aldhizer & Weaver v. Savin Corp., 350 S.E.2d 635, 637 (Va. 1986)(same).

[253] *See* Mieske v. Bartell Drug Co., 593 P.2d 1308, 1311 (Wash. 1979).

[254] *See* McGregor v. Dimou, 422 N.Y.S.2d 806, 811 (N.Y. Civ. Ct. 1979)(discussion of buyer's duty to mitigate damages); R.I. Lampus Co. v. Neville Cement Prod. Corp., 336 A.2d 397, 407 (Pa. Super Ct. 1975)(same), *aff'd* 378 A.2d 288 (Pa. 1977).

[255] *See* Cates v. Morgan Portable Bldg. Corp., 780 F.2d 683, 688-89 (7th Cir. 1985); Catlin Aviation Co. v. Equilease Corp., 626 P.2d 857, 861 (Okla. 1981).

[256] *Cates*, 780 F.2d at 869. *See also* Larry Goad & Co. v. Lordstown Rubber Co., 560 F. Supp. 583, 588 (E.D. Mo. 1983); Indiana Farm Bureau Coop. Ass'n v. S.S. Sovereign Faylenne, 24 U.C.C. Rep. Serv. (Callaghan) 74 (S.D.N.Y. 1977); *Catlin Aviation*, 626 P.2d at 861; V. Zappala & Co. v. Pyramid Co. 439 N.Y.S.2d 765, 767 (1981).

Although the Code is silent on the point, most courts have held that the burden is on the seller to prove that the buyer has unreasonably failed to mitigate damages arising from accepted goods.[260]

IV. Conclusion

Section 2-174 is a curious provision when compared with the other Code damage provisions and is certainly no model of the draftsman's art. It begins with a subsection which has virtually no range of transactions to which it logically applies. It ends with a crescendo by allocating an entire subsection to incidental and consequential damages, unlike other Code damage provisions which merely include these special damages as part of the general damage formulae. In between, in subsection (2), it states a quite specific damage measurement applicable to the broad range of cases but then appends to it, almost as an afterthought, a "special circumstances" exception with the potential to swallow the specific rule. Despite this potential for chaos, it nevertheless has presented little difficulty for the courts, which have interpreted it to compensate buyers who retain contracted goods. As with the significant majority of Article Two provisions, section 2-714 has proved to be readily manipulable and capable of being sensibly accommodated to the situations it was intended to address.

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[257] *See Cates*, 780 F.2d at 688-89; *see also* R.E.B., Inc. v. Ralston Purina Co., 525 F.2d 749, 755-56 (10th Cir. 1975)(statement of rule on buyer's duty to mitigate); Sauers v. Tibbs, 363 N.E.2d 444, 449 (Ill. App. Ct. 1977)(same); Holm v. Hansen, 248 N.W.2d 503, 510-11 (Iowa 1976)(same); Schatz Distributing Co. v. Olivetti Corp. of Am., 647 P.2d 820, 827 (Kan. Ct. App. 1982)(same); Barnard v. Compugraphic Corp., 667 P.2d 117, 120 (Wash. Ct. App. 1983)(same).

[258] *See R.E.B., Inc.*, 525 F.2d at 756.

[259] *Cates*, 780 F.2d at 686-87.

[260] *See Cates*, 780 F.2d at 688; *see also* Clark v. International Harvester Co., 581 P.2d 784, 805 (Idaho 1978)(burden to prove that damages could have been minimized on defendant); Ambassador Steel Co. v. Ewald Steel Co., 190 N.W.2d 275, 280 (Mich. Ct. App. 1971)(same); Eager v. Siwek Lumber & Millwork, Inc., 392 N.W.2d 691, 694-95 (Minn. Ct. App. 1986)(same); Hepper v. Triple U Enterprises, 388 N.W.2d 525, 530 (S.D. 1986)(same).

ACCOUNTANTS' LIABILITY IN AN INDETERMINATE AMOUNT FOR AN INDETERMINATE TIME TO AN INDETERMINATE CLASS: AN ANALYSIS OF *TOUCHE ROSS & CO. V. COMMERCIAL UNION INS. CO.*

*Denzil Y. Causey, Jr.**

American jurisdictions are increasingly divided as to the accountant's duty to exercise reasonable care for the benefit of a non-client third-party. This diversity encourages plaintiffs to engage in forum shopping whenever a loss transaction involves several jurisdictions. Thus, the accountant's responsibility may ultimately depend upon fortuitous events that suffice to invoke the law of a particular jurisdiction.

In 1987 the Mississippi Supreme Court decided *Touche Ross & Co. v. Commercial Union Insurance Co.*,[1] that adds still more diversity to the law. All nine justices concurred in adopting a rule making the independent auditor "liable to reasonably foreseeable users of the audit, who request and receive a financial statement from the audited entity for a proper business purpose, and who then detrimentally rely on the financial statement, suffering a loss, proximately caused by the auditor's negligence."[2] This distinction, whereby the auditor owes a duty of care to all who obtain a firm's financial statement directly from the audited entity, but owes no such duty of care to those who obtain it from an annual report in a library, or from a government file, makes Mississippi and New Jersey unique among courts that have considered the matter.

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[1] 514 So. 2d 315 (Miss. 1987).

The purpose of this article is to review the standard of care and the scope of duty imposed by American jurisdictions upon accountants and then to present a comparative analysis of the results and issues presented by the Mississippi Supreme Court's decision in *Touche Ross*. This article first examines the diverse views taken by other jurisdictions and the effect of each of the following factors in determining the scope of the duty and the standard of care for public accounting practice in various jurisdictions:

- The Relationship of the Parties;
- The Theory of Suit; and
- The Particular Criteria Selected to Measure Due Professional Care.

The decision in *Touche Ross* is then analyzed and compared with the decisions of other American jurisdictions. The article concludes with the author's proposal for the direction that the courts and legislatures should take to promote a public policy of avoiding the increasing diversity, uncertainty, and related forum shopping that now characterize the legal environment for public accounting practice.

I. THE RELATIONSHIP OF THE PARTIES

The first of four essential elements[3] in a professional malpractice case is the duty to use reasonable care, which for a professional, is the usual standard in the professional community.[4]

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[2] *Touche Ross*, 514 So.2d at 322.

[3] The four essential elements have been enumerated as: (1) the *duty* of the profession to use such skill, prudence and diligence as other members of his profession commonly possess and exercise; (2) *breach of* that *duty*; (3) a *proximate causal connection* between the negligent conduct and the resulting injury; and (4) actual loss or damage resulting from the professional negligence. Bucquet v. Livingston, 57 Cal. App. 3d 914, 920-26, 129 Cal. Rptr. 514, 518 (1976).

[4] 3 T. COOLEY, TORTS § 472 (4th ed. 1932). The responsibility of those offering spe-

Whether the accountant owes the plaintiff this common-law duty of due professional care depends upon the particular jurisdiction's evaluation of the relationship between the parties. While all jurisdictions find the duty where there is an accountant-client relationship, there is a growing diversity among the various jurisdictions as to the circumstances which give rise to a duty for the benefit of a third party. Conservative jurisdictions follow the landmark *Ultramares Corp. v. Touche*,[5] and limit the duty to relationships involving privity or to identified third parties who rely on the information in the particular transactions that the accountant intended to influence. Liberal jurisdictions impose a duty of care to anyone who could reasonably be a user of the accountant's report. Jurisdictions that follow the *Restatement (Second) of Torts*[6] occupy a position between the con-

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cial skills is stated in a frequently quoted passage from TORTS:

> In all those employments where peculiar skill is requisite, if one offers his services, he is understood as holding himself out to the public as possessing the degree of skill commonly possessed by others in the same employment, and if his pretensions are unfounded, he commits a species of fraud upon every man who employs him in reliance on his public profession. But no man, whether skilled or unskilled, undertakes that the task he assumes shall be performed successfully, and without fault or error; he undertakes for good faith and integrity, but not for infallibility, and he is liable to his employer for negligence, bad faith, or dishonesty, but not for losses consequent upon mere errors of judgment.

Id.

[5] 255 N.Y. 170, 174 N.E. 441 (1931).

[6] 3 RESTATEMENT (SECOND) OF TORTS § 552 (1977). Section 552 provides:

> TOPIC 3. NEGLIGENT MISREPRESENTATION
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> (1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.
>
> (2) *Except as stated in Subsection (3), the liability stated in Subsection (1) is limited to loss suffered*
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> (a) *by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and*
>
> (b) *through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.*
>
> The liability of one who is under a public duty to give the information extends to loss suffered by any of the class of persons for whose benefit the duty is

servative and liberal extremes, and impose a duty of care only to a "limited group of persons" in connection with types of transactions that the accountant intended to influence.[7]

A. *Jurisdictions Following Ultramares*

Colorado,[8] Florida,[9] Indiana,[10] New York,[11] and one court applying Pennsylvania law[12] are at the most conservative end of the spectrum, and have not moved very far from the 1931 landmark decision of *Ultramares v. Touche.*[13] Florida holds rigidly to the *Ultramares* rule that an accountant owes a duty of

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created, in any of the transactions in which it is intended to protect them. *Id.* (emphasis added).

[7] *Id.*

[8] *E.g.*, Stephens Indus., Inc. v. Haskins & Sells, 438 F.2d 357, 360 (10th Cir. 1971). In *Stephens*, the federal court reasoned that Colorado law imposed no duty of protecting the primary beneficiary of the audit who was identified to the auditor as the purchaser of corporate stocks. *Id.* at 361.

[9] *E.g.*, Canaveral Capital Corp. v. Bruce, 214 So. 2d 505, 505 (Fla. Dist. Ct. App. 1968). The court held that the liability of an accountant to a third party required a showing of either gross negligence or that a fraudulent accountant knew of the third party's intended reliance. *Id.*

[10] *E.g.*, Toro Co. v. Krouse, Kern & Co., 827 F.2d 155, 157-58 (7th Cir. 1987). The court upheld the district court's grant of summary judgment for the accounting firm on the grounds that it owed no duty of care to a third party creditor where there had been no conduct linking the accounting firm and the third party which showed that the accountant understood that the third party intended to rely. *Id.* at 158. The court followed the strict doctrine announced by the New York Court of Appeals in Credit Alliance v. Arthur Anderson & Co., 65 N.Y.2d 536, 483 N.E.2d 110, 118, 493 N.Y.S.2d 435, 443 (1985). *Toro Co.*, 827 F.2d at 157-58.

[11] *E.g.*, William Iselin & Co. v. Landau, 128 A.D.2d 453, 513 N.Y.S.2d 3, 4 (1987)(factor who had made large loans to suit and sportswear manufacturer had no action for negligence against manufacturer's accounting firm because reports issued were "review" reports which expressed no opinion on financial statements); Credit Alliance v. Arthur Anderson & Co., 65 N.Y.2d 536, 553, 483 N.E.2d 110, 119, 493 N.Y.S.2d 435, 444 (1985)(lender and borrower's accountant were not in relationship of privity sufficient to establish accountant's liability for negligence because plaintiff failed to allege either that purpose of accountant's employment was to induce lender to extend credit or that accountant had any direct dealings with lender); Ultramares Corp. v. Touche, 255 N.Y. 170, 174 N.E. 441 (1931)(action for fraud by lender sustained against defendant-accountant when evidence disclosed that ledger entry not supported in the journal and there was reason for suspicion because of inflated inventories).

[12] *E.g.*, Hartford Accident and Indem. Co. v. Parente, Randolph, Orlando, Carey & Assoc., 642 F. Supp. 38, 40 (M.D. Pa. 1985)(federal court held Pennsylvania law requires privity to maintain claim for professional malpractice).

[13] 255 N.Y. 170, 174 N.E. 441 (1931).

care only to the client; consequently, third parties must prove intentional or reckless misrepresentation in order to recover.[14] New York reaffirmed the *Ultramares* rule in *Credit Alliance v. Authur Anderson & Co.*[15] and in doing so formulated the following criteria which must be met before imposing a duty of care to third parties:

> Before accountants may be held liable in negligence to noncontractual parties who rely to their detriment on inaccurate financial reports, certain prerequisites must be satisfied: (1) the accountants must have been aware that the financial reports were to be used for a particular purpose or purposes; (2) in the furtherance of which a known party or parties was intended to rely; and (3) there must have been some conduct on the part of the accountants linking them to that party or parties, which evinces the accountants' understanding of that party or parties' reliance.[16]

The *Ultramares* case had held that there was no duty of care to a third-party lender who was not a creditor at the date of the balance sheet.[17] In *Credit Alliance* the nexus was a step closer because the plaintiff was a creditor of the client at the time of the audit, and claimed to have relied on the audit in extending and renewing credit.[18] Thus, neither a future (as in *Ultramares*) nor pre-existing (as in *Credit Alliance*) creditor is owed a duty of care in New York unless the specific criteria are met. In a later case, the New York court showed the strictness of its standard by holding that an auditor who understood that the purpose of the audit was to obtain a loan from "Drexel" owed no duty of care to "Westpac" who actually made the loan.[19]

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[14] *See* Gordon v. Etue, Wardlaw & Co., P.A., 511 So. 2d 384 (Fla. Dist. Ct. App. 1987)(court certified question of third-party liability as question of great public importance); *see also* Nortek, Inc. v. Alexander Grant & Co., 532 F.2d 1013, 1015 (5th Cir.)(accounting firm not liable for negligence in absence of privity), *cert. denied*, 429 U.S. 1042 (1967); Investors Tax Sheltered Real Estate, Ltd. v. Laventhol, Kerkstein, Horwath & Horwath, 370 So. 2d 815, 817 (Fla. Dist. Ct. App. 1970)(third party must establish either gross negligence or knowledge of reliance accompanied by fraud); Dubbin v. Touche Ross & Co., 324 So. 2d 128, 129 (Fla. Dist. Ct. App. 1975)(dismissal of malpractice suit against accounting firm based on third-party beneficiary theory affirmed on appeal); Canaveral Capital Corp. v. Bruce, 214 So. 2d 505, 505-06 (Fla. Dist. Ct. App. 1968)(accountants not liable for third-party loss absent proof of gross negligence or knowledge that third party intended to rely on statements); Investment Corp. of Fla. v. Buchman, 208 So. 2d 291, 295-96 (Fla. Dist. Ct. App. 1968)(accountants not liable to foreseen user of negligently prepared financials where third-party beneficiary relationship found absent). *Contra* Seaboard Sur. Co. v. Garrison, Webb & Stanaland, P.A., 823 F.2d 434 (11th Cir. 1987)(third-party beneficiary theory approved but tort theory rejected).

[15] 65 N.Y.2d 536, 551, 483 N.E.2d 110, 118, 493 N.Y.S.2d 435, 443 (1985).

[16] *Credit Alliance*, 65 N.Y.2d at 551, 483 N.E.2d at 118, 493 N.Y.S.2d at 443. In William Iselin & Co. v. Landau, 128 A.D.2d 453, 513 N.Y.S.2d 3, 4 (1987), the court dismissed a third-party factor's negligence suit against an accounting firm because (1) the *Credit Alliance* test was not met, and (2) there was no reliance or causation because the accountant's engagement was limited to a review expressing no opinion and the factor made its own analysis of the company. *Id.*

Several states have also adopted this conservative approach by enacting statutes. Those states which have adopted statutes placing them on similar footing with New York include Arkansas, Illinois and Kansas. The Illinois statute states:

> No person, partnership or corporation licensed or authorized to practice under this Act or any of its employees, partners, members, officers or shareholders shall be liable to persons not in privity of contract with such person, partnership or corporation for civil damages resulting from acts, omissions, decisions or other conduct in connection with professional services performed by such person, partnership or corporation, except for:
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> (1) such acts, omissions, decisions or conduct that constitute fraud or intentional misrepresentations, or
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> (2) such other acts, omissions, decisions or conduct, if such person, partnership or corporation was aware that a primary intent of the client was for the professional services to benefit or influence the particular person bringing the action; provided, however, for the purposes of this subparagraph (2), if such person, partnership or corporation (i) identifies in writing to the client those persons who are intended to rely on the services, and (ii) sends a copy of such writing or similar statement to those persons identified in the writing or statement, then such person, partnership or corporation or any of its employees, partners, members, officers or shareholders may be held liable only to such persons intended to so rely, in addition to

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[17] Ultramares Corp. v. Touche, 255 N.Y. 170, 174 N.E. 441, 444-48 (1931).

[18] *Credit Alliance*, 65 N.Y.2d at 540, 493 N.Y.S.2d at 436, 483 N.E.2d at 111.

[19] Westpac Banking Corp. v. Deschamps, 66 N.Y.2d 16, 19, 484 N.E.2d 1351, 1352-53, 494 N.Y.S.2d 848, 849-50 (1985).

> those persons in privity of contract with such person, partnership or corporation. (Effective August 6, 1986).[20]

The Arkansas statute is virtually identical to the above quoted Illinois statute.[21] The approach taken by Arkansas and Illinois provides a loophole by affording plaintiffs the option of alleging that a primary intent of the client was to benefit the plaintiff. In order to avoid this loophole, the accountant must identify in writing the persons who are intended to rely on the services provided, and thereby cut off negligence liability to all others. Thus, it becomes extremely important for accountants practicing in either Arkansas or Illinois to address this matter in writing and thereby avoid liability to all but the named parties. However, as a practical matter, this is no solution because all important parties involved will insist upon being named as beneficiaries in the statement.

The Kansas statute[22] leaves no loophole for allegations of

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[20] ILL. ANN. STAT. ch 111, ¶ 5535.1 (Smith-Hurd Supp. 1987).

[21] ARK. STAT. ANN. § 16-114-302 (Supp. 1987). The Arkansas statute provides:

> No person, partnership or corporation licensed or authorized to practice under the Public Accountancy Act of 1975 . . . or any of its employees, partners, members, officers, or shareholders shall be liable to persons not in privity of contract with such person, partnership or corporation for civil damages resulting from acts, omissions, decisions, or other conduct in connection with professional services performed by such person, partnership or corporation, except for:
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> (1) Acts, omissions, decisions or conduct that constitutes fraud or intentional misrepresentations, or
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> (2) Other acts, omissions, decisions or conduct, if the person, partnerships or corporation was aware that a primary intent of the client was for the professional services to benefit or influence the particular person bringing the action. For the purpose of this subdivision, if the person, partnership or corporation: (A) Identifies in writing to the client those persons who are intended to rely on the services, and (B) Sends a copy of the writing or similar statement to those persons identified in the writing or statement, then the person, partnership, or corporation or any of its employees, partners, members, officers, or shareholders may be held liable only to the persons intended to so rely, in addition to those persons in privity of contract with such person, partnership or corporation. (Effective 4/6/87)

Id.

[22] KAN. STAT. ANN. § 1-402 (Supp. 1987). The Kansas statute provides:

> No person, proprietorship, partnership, professional corporation or association authorized to practice as a certified public accountant pursuant to article 3 of chapter 1 of the Kansas Statutes Annotated, or any employee, agent, partner,

primary beneficiary status, nor does it require any action by the accountant to close the loophole. It limits liability for professional negligence to the person who engaged the accountant and to those situations where both the persons and transactions were identified in writing prior to the engagement or by agreement with the accountant at a subsequent date. A Kansas accounting firm approached for approval of an additional party after the time of the engagement would be prudent to insist upon an additional fee for review of all subsequent events that might affect its prior work and also of other facts that could affect its liability to the additional party.

B. *Jurisdictions Imposing Duty to All*

At the liberal end of the spectrum are several jurisdictions which hold that an accountant owes a duty of care to anyone who could reasonably become a user of the accountant's report. Those states following this liberal view include California,[23] Minnesota,[24] Mississippi,[25] New Jersey,[26] Ohio,[27] Wisconsin,[28]

> officer, shareholder or member thereof, shall be liable to any person or entity for civil damages resulting from acts, omissions, decisions or other conduct amounting to negligence in the rendition of professional accounting services unless:
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> (a) The plaintiff directly engaged such person, proprietorship, partnership, corporation or association to perform the professional accounting services; or
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> (b)(1) the defendant knew at the time of the engagement or the defendant and the client mutually agreed after the time of the engagement that the professional accounting services rendered the client would be made available to the plaintiff, who was identified in writing to the defendant; and (2) the defendant knew that the plaintiff intended to rely upon the professional accounting services renderd the client in connection with specified transactions described in writing. (Effective 7/1/87)

Id.

[23] *E.g.*, International Mortgage Co. v. John P. Butler Accountancy Corp., 177 Cal. App. 3d 806, 820, 223 Cal. Rptr. 218, 227 (1986). An auditor owes a duty of care to classes of persons who could reasonably be recipients of an audit report. *Id.*

[24] *E.g.*, Bonhiver v. Graff, 311 Minn. 111, 248 N.W.2d 291, 302 (1976). The court found that a duty of care was owed to a third-party insurance agent who was unknown to the CPA performing bookkeeping services. *Id.*; *see* First Nat'l Bank of Minneapolis v. Kehn Ranch, Inc., 394 N.W.2d 709, 720 (S.D. 1986)(court applied Minnesota law and permitted third party to sue accounting firm for negligence; jury found no damages under state's comparative fault statute).

[25] *Touche Ross & Co.*, 514 So. 2d at 322. The court found a duty of care to those obtaining a report from an audited entity. *Id.*

and one of two Texas jurisdictions that are now divided on the issue.[29]

C. *Jurisdictions Following the* RESTATEMENT

Jurisdictions that fall somewhere between the two extremes tend to follow the *Restatement (Second) of Torts*,[30] which imposes a duty of due care only where the accountant intends the report to influence a limited group of third parties in connection with a particular transaction or a substantially similar transaction. Jurisdictions following the RESTATEMENT include Canada,[31] Georgia,[32] Iowa,[33] Kentucky,[34] Missouri,[35] Nebraska,[36] New

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[26] H. Rosenblum, Inc. v. Adler, 93 N.J. 324, 461 A.2d 138, 153 (1953). The court held that an allegation of an auditor's negligence by purchasers of stock in a publicly traded corporation was a valid claim; the auditor owed a duty of care to all those who could reasonably be recipients of his financial statements provided the statements were obtained directly from the business entity and were used to influence a business decision. *Id.*

[27] Haddon View Instrument Co. v. Coopers & Lybrand, 70 Ohio St. 2d 154, 436 N.E.2d 212, 214-15 (1982). An auditor owed a duty of care to future investors in a limited partnership. *Id.* at 215. *Contra* BancOhio National Bank v. Schiesswhol, 33 Ohio App. 3d 329, 330, 515 N.E.2d 997, 998 (Ct. App. 1986)(court interpreted *Haddon View* as application of RESTATEMENT (SECOND) OF TORTS and upheld directed verdict for accounting firm).

[28] Citizens State Bank v. Timm, Schmidt & Co., 113 Wis. 2d 376, 335 N.W.2d 361, 366 (1983). The court ruled that unless there existed a public policy reason to limit liability an accounting firm owed a duty of care to a third-party bank creditor. *Id.* In Wisconsin it is not necessary to prove reliance in an action for negligent misrepresentation. *See* Imark Industries, Inc. v. Arthur Young & Co., 141 Wis. 2d 114, 414 N.W.2d 57, 64-65 (Ct. App. 1987).

[29] Blue Bell, Inc. v. Peat, Marwick, Mitchell & Co., 715 S.W.2d 408, 412 (Tex. Ct. App. 1986). In reversing a dismissal of a negligent misrepresentation suit against an accounting firm, the court rejected the RESTATEMENT limitation of liability for negligent misrepresentation to third parties known to the accountant. *Id.* The court expressed approval of cases extending liability to all third parties who may reasonably be injured by the negligence of an accountant. *Id.* at 412-13.

[30] 3 RESTATEMENT (SECOND) OF TORTS § 552 (1977). *See supra* note 6.

[31] Haig v. Bamford, 53 D.L.R.3d 85, 94 (Can. 1974). The court ruled that chartered accountants were liable for negligence when they knew that the audited financial statements would be used to raise equity capital, but did not know the identity of the principal investor. *Id.* at 93-94.

[32] Badische Corp. v. Caylor, 257 Ga. 131, 356 S.E.2d 198, 199-200 (1987). The court rejected the plaintiffs' argument that accountants are liable for negligence to an unlimited class of persons whose presence is foreseeable. *Id.* at 200. It limited negligence liability to "those persons, or the limited class of persons who the professional is actually aware will rely on the information he prepared." *Id.* This had the result of eliminating

Hampshire,[37] North Carolina,[38] Rhode Island,[39] one of the two divided Texas courts,[40] Utah,[41] and Washington.[42] Courts have

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liability to creditors who alleged that the accountant failed to disclose that various banks had security interests in inventory. *Id.* at 199-200.

[33] Briggs v. Sterner, 529 F. Supp. 1155, 1176-77 (S.D. Iowa 1981)(accountant's liability for negligence limited to foreseen persons accountant intended to influence); Pahre v. Auditor of the State of Iowa, 422 N.W.2d 178 (Iowa 1988)(claim by guaranty company dismissed because plaintiff was not within class protected by RESTATEMENT; no discussion of any claim as subrogee). *Contra* Ryan v. Kanne, 170 N.W.2d 395, 403 (Iowa 1969)(CPA who negligently prepared balance sheet held liable to subsequently formed corporation).

[34] Ingram Indus., Inc. v. Nowicki, 527 F. Supp. 683, 684 (E.D. Ky. 1981). In denying the accounting firm's motion to dismiss, the court indicated that the plaintiff would have to prove foreseeability on the basis established in the RESTATEMENT in order to recover for negligence. *Ingram*, 527 F. Supp. at 684.

[35] Aluma Kraft Mfg. Co. v. Elmer Fox & Co., 493 S.W.2d 378, 383 (Mo. Ct. App. 1973). The court held that the complaint was valid where it alleged that negligent auditors knew their report would be used to determine the book value to be paid by plaintiff for Aluma Kraft's stock. *Id.* However, there is no liability for negligence to unidentified third parties. *Id.* at 384; *see also* Biben v. Card, [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH)¶ 92,010, at 91004-05 (W.D. Mo. 1985)(purchasers of stock not "limited group" as to impose liability on accounting firm); 999 v. Cox & Co., 574 F. Supp. 1026, 1031 (E.D. Mo. 1983)(privity not requisite for malpractice action against accountant).

[36] Seedkem, Inc. v. Sanfranek, 466 F. Supp. 340, 344-45 (D. Neb. 1979). The court refused to dismiss a negligence action by a third party alleging negligence by a CPA who maintained books and records and also issued an unaudited disclaimer. *Id.* at 341, 344-45. The plaintiff alleged that the CPA foresaw or should have foreseen the plaintiff's use of the financial statement in extending credit. *Id.* at 341.

[37] Spherex, Inc. v. Alexander Grant & Co., 122 N.H. 848, 451 A.2d 1308, 1312 (1982). In *Spherex* the court reasoned that an accounting firm may be held liable to foreseeable third parties for negligence in preparing unaudited financial statements. *Id.*

[38] Raritan River Steel Co. v. Cherry, Bekaert & Holland, 322 N.C. 200, 367 S.E. 2d 609, 617 (1988). In order to recover for *negligence* plaintiffs must prove that they relied upon the entire report including opinion and footnotes as opposed to summarized data from credit reporting services. *Id.* at 612-13.

[39] Rhode Island Hosp. Trust Nat'l Bank v. Swartz, Bresenoff, Yavner & Jacobs, 455 F.2d 847, 851 (4th Cir. 1972). Applying Rhode Island law, the court held that auditors may be liable for negligence to foreseen and limited classes. *Id.*; *see* Rusch Factors, Inc. v. Levin, 284 F. Supp. 85, 93 (D.R.I. 1968)(CPA who knows financials prepared for lender's use may be liable to lender for negligence).

[40] Shatterproof Glass Corp. v. James, 466 S.W.2d 873, 880 (Tex. Ct. App. 1971). Where an auditor was advised that the purpose of the audit was for the purpose of a particular creditor, the auditor was required to use ordinary care for that creditor's benefit. *Id.*

[41] Milliner v. Elmer Fox & Co., 529 P.2d 806, 808 (Utah 1974). The court held that there was no liability for negligence to unidentified future purchasers of corporate stock. *Id.*

[42] Haberman v. Public Power Supply Sys., 109 Wash. 2d 107, 744 P.2d 1032 (Wash.

little difficulty finding that the limited-group test is met where the plaintiff is a creditor and the accountant knew that the report was to be used by the creditor in reaching a credit decision.[43] Similarly, a sole buyer of all the corporate stock[44] or an investor in a private placement meets this test.[45] However, where the plaintiffs are unforeseen purchasers of the corporate stock, they generally do not meet the limited-group test.[46]

II. The Theory of Suit

The theories most frequently used in suits against accounting firms are summarized in Exhibit 1. The effect of each of these theories on the standard of care is discussed below.

1987). The court required a factual determination as to whether attorneys, accountants, and engineers knew that allegedly false representations concerning feasibility of nuclear power plants would be included in documents supplied to investors. *Id.*

[43] *See, e.g., Shatterproof Glass Corp.*, 466 S.W.2d at 880. An auditor who knew that an audit was for the use of a particular creditor owed a duty of care to that creditor. *Id.*; *see also Rusch Factors, Inc.*, 284 F. Supp. at 92-93 (CPA owed duty of care to foreseen lender).

[44] *See Ingrahm Indus., Inc.*, 527 F. Supp. at 684 (applying Kentucky law, accountant owed duty to foreseen purchaser of corporate stock); *see also Aluma Kraft Mfg. Co.*, 493 S.W.2d at 383 (duty owed where accountant allegedly knew that audited book value would be paid by identified purchaser of corporate stock).

[45] Haig v. Bamford, 53 D.L.R.3d 85, 94 (Can. 1974).

[46] *See* Koch Indus., Inc. v. Vosko, 494 F.2d 713, 724-25 (10th Cir. 1974)(applying Kansas law, no duty to unforeseen purchaser); *see also* Stephens Indus., Inc. v. Haskins & Sells, 438 F.2d 357, 358-60 (10th Cir. 1971)(applying Colorado law, no duty to unforeseen investor who purchased corporate stock); Briggs v. Sterner, 529 F. Supp. 1155, 1163, 1177 (S.D. Iowa 1981)(no duty to unforeseen purchasers of notes and debentures); MacNerland v. Barnes, 129 Ga. App. 467, 199 S.E.2d 564, 565-67 (1973)(no duty to purchaser of common stock where uncertified financial statement contained disclaimer opinion and purchaser was not in privity with accountant); Milliner v. Elmer Fox & Co., 529 P.2d 806, 808 (Utah 1974)(no duty to unforeseeable future purchaser of common stock). *But see* Merit Ins. Co. v. Colao, 603 F.2d 654, 659 (7th Cir. 1979), *cert. denied*, 445 U.S. 929 (1980)(court held that new underwriter sought by insurance agent client was protected member of limited class).

EXHIBIT 1

Principal Theories of Civil Suits Against Accountants

Plaintiff	Theory of Recovery	Damages
Purchaser of Unregistered Securities	Absolute Liability Under State Blue Sky or § 12(1) of the Securities Act	Rescission or Out-of-Pocket Loss
Clients or Third Parties Protected Under State Law	Common-Law Breach of Contract or Negligence (Failure to Apply Usual Professional Standard, or Standard Applicable to Specialty or Fiduciary Relation)	Benefit of Bargain, Out of Pocket Loss, or Rescisson
Anyone Who Loses After Reliance	Fraud Under Common Law	Out-of-Pocket Loss
Purchasers or Sellers of Securities	Fraud Under Federal Securities Laws	Out-of-Pocket Loss
Anyone Who Relies and Loses	Pattern of Mail or Securities Fraud Under RICO	Triple the Loss Plus Attorney Fees

A. *Securities Laws Imposing Absolute Liability*

Both state and federal laws impose liability on sellers of unregistered securities and those who aid and abet their sale. The purchasers are given the right to rescind the sale and be restored to the former position or to sue for damages. Accountants have been held liable under a state blue-sky law imposing liability for aiding and abetting the sale of unregistered securities despite absence of any proof of misrepresentation.[47] Where accountants have become actively involved in the selling of unregistered securities, liability without fault may be imposed under section

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[47] *E.g.*, Hild v. Woodcrest Ass'n, 59 Ohio Misc. 2d 13, 391 N.E.2d 1047, 1056-57 (C.P. Montgomery County 1977). In *Hild*, an accounting firm prepared financial and investment information in preparation for a public offering of interests in a limited partnership that was found to be violative of state securities laws. *Id.* at 1049, 1053. The accountants were found to have "participated or aided" in the sale within the meaning of the state Securities Act, subjecting the firm to liability for violation of securities registration procedures. *Id.* at 1057.

12(1) of the Securities Act of 1933.[48] In *Jenson v. Touche Ross & Co.*[49] the court held that Minnesota's Consumer Fraud Act does not impose liability without fault on accounting firms.[50]

Investors in a new issue of securities *registered* under the Securities Act of 1933 can recover from accountants under section 11(a) of the Act.[51] In order to avoid liability, the *accountants must prove due diligence* in ascertaining the accuracy of the representations at the time the registration statement became effective.[52] While this is not as onerous as the liability without fault discussed above, the shifting of the burden of proof makes defense of a case involving material financial misrepresentations difficult and doubtful.[53]

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[48] En Yun Hsu v. Leaseway Trans. Corp., [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH)¶ 92,043, at 91, 199 (N.D. Cal. March 29, 1985). In *En Yun Hsu* the plaintiffs brought suit against their accountants, upon whom they had relied for accounting services and financial advice for a period of seven years. *Id.* at 91, 197. Accountants advised them to invest in a truck leasing service involving the purchase and lease of a new sixty-thousand dollar truck; further, the accountants assumed responsibility for initiating and managing the service in the plaintiffs' absence. *Id.* The accountants subsequently purchased a used truck, forged the plaintiffs' signatures to various documents, and generally mismanaged the leasing service to the plaintiffs' detriment. *Id.* at 91,197-98. Plaintiffs successfully sued, establishing breach of fiduciary duty, malpractice, and violation of the Securities Act of 1933. *Id.* at 91, 201-02.

[49] 335 N.W.2d 720 (Minn. 1983).

[50] *Jensen*, 335 N.W.2d at 728. The court found that any misrepresentation must have been knowingly made by the accountants, and that in the absence of a showing of some culpability, accountants could not be held liable under a consumer fraud statute. *Id.*; *accord* Haberman v. Washington Pub. Power Supply Sys., 109 Wash. 2d 107, 169, 744 P.2d 1032, 1071 (Wash. 1987)(claims relating to the substantive quality of professional services, as opposed to entrepreneurial aspects, are not actionable under Consumer Protection Act); Robertson v. White, 633 F. Supp. 954, 978 (W.D. Ark. 1986)(Arkansas and Oklahoma Consumer Protection Acts are not designed to regulate lawyer-client or accountant-client relationships).

[51] *See, e.g.*, Escott v. BarChris Constr. Corp., 283 F. Supp. 643, 697-98 (S.D.N.Y. 1968). In *Escott*, the accounting firm of Peat, Marwick, Mitchell & Co. was found liable under the Securities Act of 1933 § 11(a), 15 U.S.C. § 77k(a)(4)(1982) in connection with material misstatements. *Id.*

[52] *See* Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 369-70 (2nd Cir.), *cert. denied*, 414 U.S. 910 (1973)(for suit brought under section 11(a) of Securities Act of 1933, due diligence defense under § 11(b) is available to all but issuer of securities). A "due diligence" defense absolves a defendant of liability upon establishing that:

> [H]e had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to make the statements therein not misleading.

Securities Act of 1933, § 11(c), 15 U.S.C. § 77k(b)(3)(B)(i)(1982).

B. Common-Law Contract, Negligence, and Fiduciary Theories

While the accountant's duty to apply due professional care for the benefit of non-client third parties depends upon the diverse law of the various states, *recovery for breach of contract* should be limited to *clients* or primary beneficiaries of the contract with the client. Apparently North Carolina[54] and Florida[55] are the only jurisdictions that have recognized third-party recovery based on the contract theory. While both contract and negligence theories impose a duty to use due care for the client's benefit, there may be differences in the measure of damages and available defenses, such as the statute of limitations.[56]

If the plaintiff's negligence or contract theory is based on a fiduciary breach by the accountant, the court may apply a higher standard of care for measuring the accountant's conduct or give the plaintiff the right to rescind the transaction.[57] As discussed below under "Criteria," a fiduciary has the burden of proving the highest standards of candor, good faith, and fairness,[58] while a specialist (or a person undertaking a specialty) may be held in some jurisdictions to the standard for the specialist.[59] In *Robertson v. White*[60] the court held that accountants and attorneys who assist a fiduciary, i.e. management, in the breach of fiduciary duties are liable to the corporate trustee in bankruptcy for damages to the entity and are liable to investors for damage relating to wrongfully prolonging the operations.

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[53] *See, e.g., Escott*, 283 F. Supp. at 683. *See supra* note 51.

[54] Raritan River Steel Co. v. Cherry, Bekaert & Holland, 79 N.C. App. 81, 339 S.E.2d 62, 65-66 (1986), *rev'd in part and aff'd in part*, 322 N.C. 200, 367 S.E.2d 609 (1988)(where contract entered into for direct benefit of third-party lender, lender could sue for negligent misrepresentation under third-party beneficiary theory).

[55] Seaboard Sur. Co. v. Garrison, Webb & Stanaland, P.A., 823 F.2d 434, 436 (11th Cir. 1987)(per curiam)(third-party beneficiary claim by bonding company allowed but negligence theory rejected).

[56] California, Nebraska, and West Virginia courts hold that plaintiff can elect either tort or contract remedies in suits for negligent performance of professional services. *See* Heyer v. Flaig, 449 P.2d 161, 163-64 (Cal. 1969); Lincoln Grain, Inc. v. Coopers & Lybrand, 216 Neb. 433, 345 N.W.2d 300, 304-05 (Neb. 1984); Harrison v. Castro, 271 S.E.2d 774, 775 (W. Va. 1980). Alabama gives plaintiff the election where the accountant *expressly undertakes* to use due care; otherwise the Alabama suit sounds in tort. *See* Blumberg v. Touche Ross & Co., 514 So. 2d 922, 927 and n.4 (Ala. 1987). Arizona, Arkansas, Kansas, and Mississippi hold that suits for negligent performance sound exclusively in tort. *See* Sato v. Van Denburgh, 123 Ariz. 255, 599 P.2d 181, 183 (1979); Robertson v. White, 633 F. Supp. 954, 974 (W.D. Ark. 1986); Brueck v. Krings, 203 Kan. 466, 638 P.2d 904, 907 (1982); Hutchinson v. Smith, 417 So. 2d 926, 928-29 (Miss. 1982). Minnesota and New York hold the remedy is exclusively contractual. *See* City of E. Grand Forks v. Steele, 121 Minn. 296, 141 N.W. 181, 182 (1913); Video Corp. of Am. v. Frederick Flatto Assoc., Inc., 58 N.Y.2d 1026, 1028, 448 N.E.2d 1350, 1350, 462 N.Y.S.2d 439, 439 (1983). Louisiana holds that the contract limitation period can apply to attorney malpractice only where there is nonfeasance or the attorney warrants a particular result. Newsom v. Boothe, 524 So. 2d 923 (La. App. 1988). Illinois holds that a client's claim based on a written engagement letter to audit and to disclose errors and irregulatiries sounds in contract. *In re* American Reserve Corp., 79 Bankr. 729 (N.D. Ill. 1987); Holland v. Arthur Andersen & Co., 469 N.E.2d 419 (Ill. App. 1984).

Both federal and state laws recognize the stockholder's right to sue derivatively on behalf of the corporation and to enforce the corporation's right against accountants, officers and directors.[61] Some states permit limited partners to sue accountants or general partners derivatively on behalf of the limited partnership.[62] In these actions the plaintiff, who may otherwise be regarded as an unprotected third party, receives the benefit of the accountant's duty of care to the client. However, any recovery in the derivative suit goes to the corporation or to the limited partnership and only indirectly benefits the plaintiff.[63]

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[57] *See, e.g.*, Russell v. Campbell, 725 S.W.2d 739, 745 (Tex. Ct. App. 1987)(enumerating non-exclusive factors supporting finding of accountant's breach of fiduciary duty); En Yun Hsu v. Leaseway Transp. Corp., [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH)¶ 92,043, at 91,200-01 (N.D. Cal. March 29, 1985)(recission allowed upon breach of fiduciary duty).

[58] Wadsworth v. Adams, 138 U.S. 380, 389 (1890)("[L]aw requires strictest good faith upon the part of one occupying a relation of confidence to another."); Van Zandt v. Van Zandt, 227 Miss. 528, 538, 86 So. 2d 466, 470 (1956)("[F]iduciary [relationship] demands . . . the utmost loyalty and good faith . . . .").

[59] It is commonly accepted that public accountants are held to the same standards of care as found applicable to "doctors, lawyers, architects, engineers and others furnishing skilled services for compensation and that standard requires reasonable care and competence therein." Delmar Vineyard v. Timmons, 486 S.W.2d 914, 920 (Tenn. Ct. App. 1972). The First District Court of Appeals for California elaborated on this general statement, recognizing that, as members of a skilled profession, accountants are experts: "The services of experts are sought because of their special skill. They have a duty to exercise the ordinary skill and competence of members of their profession, and a failure to discharge that duty will subject them to liability for negligence." Linder v. Barlow, Davis & Wood, 210 Cal. App. 2d 660, 27 Cal. Rptr. 101, 104 (1962).

[60] 633 F. Supp. 954, 966-78, 969 (W.D. Ark. 1986).

[61] Although shareholder derivative suits are most commonly associated with suits brought against officers and directors, the action may be maintained against third parties negligently injuring the corporation if the corporation cannot, or will not, sue for relief on its own behalf. 12B W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS. § 5850 (Perm. ed. 1984); *see, e.g.*, Ruggiero v. American Bioculture, Inc., 56 F.R.D. 93 (S.D.N.Y. 1972). In *Ruggiero* the district court split a single complaint against the corporate defendant, its officers and its certified public accountants into a consolidated complaint of two distinct groups of plaintiffs; the first group was composed of section 10(b)-5

C. Common Law Fraud Theories

Plaintiffs who sue under a common-law fraud theory must prove wilful, intentional or reckless conduct, as opposed to negligence.[64] This burden has sometimes resulted in defense verdicts.[65] However, liability has been imposed where the accountants continued to supply information to a bank without disclosing the client's diversion of cash receipts.[66] Another court, applying the fraud standard, refused to dismiss a claim where it was alleged that the auditor knew, but failed to disclose, that a

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plaintiffs suing the corporation and the second was composed of corporate shareholders suing derivatively on behalf of the corporation. *Id.* at 95-96.

[62] *See* Jaffe v. Harris, 109 Mich. App. 786, 312 N.W.2d 381, 385 (1981)(substantial similarity between interests of limited partners and corporate shareholders compels conclusion that derivative cause of action exists for partners); *see also* White v. Guareute, 43 N.Y.2d 356, 361-62, 372 N.E.2d 315, 318-19, 401 N.Y.S.2d 474, 477-78 (1977)(accountant can be held liable to group of limited partners as members of known group with vested rights).

[63] Pearl v. General Tire & Rubber Co., 726 F.2d 1075, 1087 (6th Cir. 1984)(relief obtained belongs to corporation only); Recchion *ex rel.* Westinghouse Elec. Corp. v. Kirby, 637 F. Supp. 1309, 1315 n.1 (W.D. Pa. 1986)(recovery belongs to corporation).

[64] *See* Herzfeld v. Laventhol, Krekstein, Horwath & Horwath, 378 F. Supp. 112 (S.D.N.Y. 1974), *modified* 540 F.2d 27 (2d Cir. 1976). In *Herzfeld* the plaintiff recovered for damages suffered as a result of the common-law fraud perpetrated by the defendant accounting firm in connection with financial statements prepared for an issuer of securities. In order to recover, the plaintiff successfully established that: "(1) Laventhol made a false representation of material fact, (2) Laventhol knew it was false, (3) Laventhol made the representation with intent to deceive investors and to induce them to rely upon it, (4) plaintiffs did rely upon it, and (5) plaintiffs suffered damage as a result." 378 F. Supp. at 131; *see also* Berkowitz v. Baron, 428 F. Supp. 1190, 1196 (S.D.N.Y. 1977)(accounting firm held liable for financial reports materially deviating from generally accepted accounting principles (GAAP)).

[65] McLean v. Alexander, 599 F.2d 1190, 1198-99, 1202 (3rd Cir. 1979)(fraud action dismissed for failure to prove scienter); Pusser v. Gordon, 684 S.W.2d 639, 642 (Tenn. Ct. App. 1985)(recovery denied where plaintiff had actual knowledge of misrepresentation).

[66] United States Nat'l Bank v. Fought, 46 Or. App. 635, 612 P.2d 754, 758 (1980).

previously issued audit report was materially misleading.[67]

D. Federal Civil Fraud Statutes

Section 10(b) of the Securities Exchange Act of 1934[68] continues to be frequently used in suits against accountants, despite the United States Supreme Court's holding in *Ernst & Ernst v. Hochfelder*[69] that liability may be imposed only upon proof of intent to deceive, manipulate or defraud.[70] While the Court reserved decision as to whether recklessness will result in liability under this standard, lower federal courts have answered in the affirmative.[71] The remedy under section 10(b) is cumulative and may be pursued while concurrently claiming recovery under the Securities Act of 1933.[72] The standard of proof is by a preponderance of the evidence, and not the "clear and convincing" rule sometimes required to prove fraud at common law.[73] Where recision is an appropriate remedy, tax benefits that have accrued to the plaintiffs may not be used to reduce the amount of recovery.[74]

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[67] Fischer v. Kletz, 266 F. Supp. 180, 184-89 (S.D.N.Y. 1967).

[68] 15 U.S.C. § 78j (b)(1982).

[69] 425 U.S. 185 (1976).

[70] *Hochfelder*, 425 U.S. at 201. The Court held that liability could not be imposed for negligent conduct alone. *Id.* For other cases imposing liability on accountants under § 10(b), see Sharp v. Coopers & Lybrand, 649 F.2d 175, 183-84 (3d Cir. 1981), *cert. denied*, 455 U.S. 938 (1982)(where accounting firm knew reports would be used to influence investors, firm had duty to use reasonable care); Herzfeld v. Laventhol, Kerkstein, Horwath & Horwath, 540 F.2d 27, 33-34 (2d Cir. 1976)(plaintiff must prove "misrepresentation" that was "substantial factor" in securities activities).

[71] *See* McLean v. Alexander, 599 F.2d 1190, 1197 (3d Cir. 1979)("recklessness" standard applicable to misstatements, as well as to omissions); Mansbach v. Prescott, Ball & Turben, 598 F.2d 1017, 1023-25 (6th Cir. 1979)(recklessness satisfied scienter requirement); Nelson v. Serwold, 576 F.2d 1332, 1337 (9th Cir.), *cert. denied*, 439 U.S. 970 (1978)(Congress intended that § 10(b) scienter include recklessness); Rolf v. Blyth, Eastman, Dillion & Co., 570 F.2d 38, 44 (2d Cir.), *cert. denied*, 439 U.S. 1039 (1978)(recklessness satisfies scienter requirement for "aiding and abetting" liability); Sundstrand Corp. v. Sun Chem. Corp., 553 F.2d 1033, 1044-45, (9th Cir.) *cert. denied*, 435 U.S. 953 (1978)(danger of misleading buyers must be actually known). *See generally* Haimoff, *Holmes Looks at Hochfelder and 10b-5*, 32 Bus. Law. 147-75 (Nov. 1976)(analysis of recklessness as scienter).

[72] Herman & Maclean v. Huddleston, 459 U.S. 375, 382-83 (1983).

[73] *Id.* at 387-91.

[74] Randall v. Lofstgarden, 106 S. Ct. 3143, 3153-55 (1986).

E. Civil Liability Under RICO

Since the United States Supreme Court has rejected the requirement of proof of a criminal conviction as a predicate for civil liability,[75] the Racketeer Influenced Corrupt Organization Act [hereinafter RICO][76] has become one of the most frequently used methods for suing accounting firms.[77] Courts are divided as to whether the pattern of racketeering which is a predicate for liability must involve two or more separate schemes[78] or simply two or more acts involving a single scheme.[79] The standard of conduct for imposing liability is the same as for common-law fraud or for liability under Section 10(b); therefore, the result has been displacement of other theories because of the possibility of recovering treble damages plus attorneys' fees and costs.[80]

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[75] Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 488-91 (1985).

[76] 18 U.S.C. §§ 1961-1968 (1982 & Supp. 1986).

[77] *See* Bank of Am. Nat'l Trust & Savings Ass'n v. Touche Ross & Co., 782 F.2d 966, 970-71 (11th Cir. 1986)(RICO claim allowed against accounting firm); James v. Meinke, 778 F.2d 200, 207 (5th Cir. 1985)(treble damages awarded against accountant who recommended stock investment). Note, though, that RICO is a two-edged sword. One accounting firm successfully used the theory to recover for injuries suffered when a former client utilized "a pervasive scheme of mail and wire fraud designed . . . to obtain a favorable audit . . . ." Alexander Grant & Co. v. Tiffany Industries, Inc., 770 F.2d 717, 718 (8th Cir. 1985), *cert. denied*, 106 S. Ct. 799 (1986).

[78] *See* Lipin Enter., Inc. v. Lee, 803 F.2d 322, 323 (7th Cir. 1986)(allegation of conspiracy of attorney, accountants, and banks to defraud purchaser in single transaction did not constitute pattern); *In re* Energy Sys. Equip. Leasing Sec. Litig., 642 F. Supp. 718, 741 (E.D.N.Y. 1986)(thousands of fraudulent transactions over course of time involving large class of investors and entailing numerous mailings constitutes pattern); Eastern Corp. Fed. Credit Union v. Peat, Marwick, Mitchell & Co., 639 F. Supp. 1532, 1536 (D. Mass. 1986)(two phone calls and one mailing concerning single audit did not involve acts substantially separated in time or substance); Professional Assets Mgmt., Inc. v. Penn Square Bank, 616 F. Supp. 1418, 1420-21 (W.D. Okla. 1985)(pattern may not be based on single audit). *But see* Morgan v. Bank of Waukegan, 804 F.2d 970, 976 (7th Cir. 1986)(several acts of mail fraud involving single scheme constituted pattern). *See generally* Moran, *The Meaning of Pattern in RICO*, 62 CHI.[-]KENT L. REV. 139, 148-55 (1985)(discussing meaning of "pattern" and how courts have interpreted meaning of "pattern" after *Sedima*).

[79] *See* Bank of Am. Nat'l Trust & Savings Ass'n v. Touche Ross & Co., 782 F.2d 966, 970-71 (11th Cir. 1986)(RICO claim involving single scheme sufficient where accounting firm allegedly participated in mail fraud over three year period); Penturelli v. Spector Cohen Gradon & Rosen, 640 F. Supp. 868, 873-74 (E.D. Pa. 1986)(several acts to entice plaintiff into single transaction constituted pattern); Papai v. Cremosnik, 635 F. Supp. 1402, 1407-09 (N.D. Ill. 1986)(pattern consisting of concealment of cash receipts, defrauding shareholder, scheming to defraud Internal Revenue Service and multiple acts of mail fraud satisfied "multiple episodes plus ongoing course of conduct" test); James v. Meinke, 606 F. Supp. 125, 126-27 (N.D. Tex. 1984), *modified*, 778 F.2d 200 (5th Cir. 1985)(two predicate offenses, specifically fraud in sale of securities, sufficient to establish pattern).

III. The Criteria for Due Professional Care

The standard for evaluating due professional care depends upon the application of one or more of the following criteria:

(a) Ethics Rules as Standards;
(b) The Fiduciary Standard of Care;
(c) Higher Standards for Specialists;
(d) National versus Local Standards;
(e) Probative Effect of Expert Testimony; and
(f) Breach of the Defendant's Standards.

A. *Ethics Rules As Standards*

Several Courts have held that the standard of care for accounting practice is established by the American Institute of Certified Public Accountants (AICPA).[81] The AICPA ethics code contains three major provisions that require public accountants to adhere to technical standards:

- Ethics Rule 202 requires auditors to comply with generally accepted auditing standards promulgated by the AICPA's Auditing Standards Board;[82]

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[80] 18 U.S.C. § 1964(c)(1982). *See, e.g., Meinke*, 778 F.2d at 201, 206-07. *Meinke* is of interest as the plaintiffs were not injured directly by the predicate offenses precipitating the RICO claim. The claim was founded upon violation of § 10(b) of the Securities Exchange Act of 1934. *Id.* at 201. Evidence established that the market value of the securities did not diminish from the time of their fraudulently induced sale. *Id.* The court of appeals rejected the defendant's defense that a lack of "out-of-pocket" damages precluded a Rule 10b-5 violation, thereby negating allegations of RICO violations, on the grounds that the plaintiffs suffered significant *consequential* damages resulting from personal guarantees of company loans. *Id.* at 206. Accordingly, the court of appeals affirmed the trial court's award of consequential damages, trebled, and attorney's fees. *Id.* at 207.

[81] *See* Rhode Island Hosp. Trust Nat'l Bank v. Swartz, Bresenoff, Yavner & Jacobs, 455 F.2d 847, 852 (4th Cir. 1972)("[w]hile industry standards may not always be the maximum test of liability, certainly that should be deemed the minimum standard"); Appalachian Power Co. v. American Inst. of Certified Pub. Accountants, 177 F. Supp. 345, 351 (S.D.N.Y.), *aff'd*, 268 F.2d 844 (2d Cir.)(per curiam), *cert. denied*, 361 U.S. 887 (1959)(court rejected challenge to AICPA's right to make rules that might impact plaintiff's financial reporting practices); Stanley L. Bloch, Inc. v. Klein, 45 Misc. 2d 1054, 258 N.Y.S.2d 501, 505-06 (N.Y. Sup. Ct. 1965)(AICPA standards bind non-members as well as members).

- Ethics Rule 203 requires an exception in audit reports for material departures from official pronouncements of the Financial Accounting Standards Board (FASB) or unsuperseded Opinions or Bulletins of its two predecessors[83]; and
- Ethics Rule 204 requires compliance with technical standards promulgated by the Management Advisory Services Executive Committee and the Accounting and Review Services Committee.[84]

There is a growing trend for courts to consider deviations from a code of professional ethics as a measure of malpractice in suits brought by clients.[85] Some courts have applied ethical standards in suits by non-clients,[86] while other courts reject ethical rules as standards in all cases.[87] In *Wagenheim v. Alexander Grant & Co.*,[88] the court found a contractual duty of an accountant to avoid disclosure of confidential client information based on the reasonable expectation of the parties that the engagement would be performed according to ethical standards. The AICPA has established a division of firms composed of a Private Companies Practice Section and an SEC Practice Section.[89] Furthermore, these sections have established quality control standards that apply to section members.[90] The legal effect of these standards upon section members, as well as upon non-members is not yet clear.

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[82] AICPA PROFESSIONAL STANDARDS, General and Technical Standards, ET § 202.01 (Am. Inst. of Certified Pub. Accountants 1978).

> Rule 202 — Auditing Standards. A member shall not permit his name to be associated with financial statements in such a manner as to imply that he is acting as an independent public accountant unless he has complied with the applicable generally accepted auditing standards promulgated by the Institute. Statements on Auditing Standards issued by the Institute's Auditing Standards Executive Committee are, for purposes of this rule, considered to be interpretations of the generally accepted auditing standards, and departures from such statements must be justified by those who do not follow them.

Id.

[83] AICPA PROFESSIONAL STANDARDS, General and Technical Standard, ET § 203.01 (Am. Inst. of Certified Pub. Accountants 1973).

> Rule 203 — Accounting Principles. A member shall not express an opinion that financial statements are presented in conformity with generally accepted accounting principles if such statements contain any departure from an accounting principle promulgated by the body designated by Council to establish such principles which has a material effect on the statements taken as a whole, unless the member can demonstrate that due to unusual circumstances the financial statements would otherwise have been misleading. In such cases his report must describe the departure, the approximate effects thereof, if practicable, and the reasons why compliance with the principle would result in a misleading statement.

Id.

[84] AICPA PROFESSIONAL STANDARDS, General and Technical Standards, ET § 204.01 (Am. Inst. of Certified Pub. Accountants 1978).

> Rule 204 — Other technical standards. A member shall comply with other technical standards, promulgated by bodies designated by Council to establish such standards, and departures therefrom must be justified by those who do not follow them.

Id.

[85] *See* Woodruff v. Tomlin, 616 F.2d 924, 935-36 (6th Cir. 1980)(attorneys' breach of

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ethical code by representing multiple clients in automobile accident without advising of conflict of interest was malpractice); Green v. Harry Savin, P.A., 455 So. 2d 494, 495 (Fla. Dist. Ct. App. 1984)(per curiam)(where accountant of doctor disclosed confidential information to doctor's wife in divorce proceedings); Lipton v. Boesky, 110 Mich. App. 589, 313 N.W.2d 163, 166-67 (1981)(violation of code of professional responsibility is rebuttable evidence of malpractice); Crawford v. Logan, 656 S.W.2d 360, 364-65 (Tenn. 1983)(attorney may forfeit right to collect fees to extent that ethics breach prejudices client).

[86] *See, e.g.*, Summer v. Land & Leisure, Inc., 571 F. Supp. 380, 386 (S.D. Fla. 1983)(allegation that auditor failed to disclose that its independence had been compromised by pledge of receivables to secure past due fees and that it would receive $50,000 in fees from public offering was sufficient to support fraud); Raine v. Drasin, 621 S.W.2d 895, 900-01 (Ky. 1981)(court relied upon expert testimony as to legal ethics in finding attorney liable for malicious prosecution); Fassihi v. Sommers, Schwartz, Silver, Swartz & Tyler, 107 Mich. App. 509, 309 N.W.2d 645, 649-50 (1981)(malpractice found where attorney failed to disclose professional affiliation with corporation and remaining shareholder to ousted shareholder in violation of ethics code).

[87] *See* Greening v. Klamen, 652 S.W.2d 730, 734 (Mo. Ct. App. 1983)(ethical rules do not enlarge the common law obligations of competence and fiduciary duty); Brainard v. Brown, 91 A.D.2d 287, 458 N.Y.S.2d 735, 738 (1983)(violation of ethics code held no basis for civil suit by client); Hilt v. Bernstein, 75 Or. App. 502, 707 P.2d 88, 93 (1985)(violation of disciplinary rule not negligence per se).

[88] 19 Ohio App. 3d 7, 482 N.E.2d 955, 963 (1983).

[89] *See* 1 AICPA PROFESSIONAL STANDARDS, The Fourth Standard of Reporting AU § 543.10 n.4 Am. Inst. of Certified Pub. Accountants 1972 (states that AICPA Divison for CPA firms can respond to inquiries about whether specific public accounting firms are members of either Private Companies Practice Section (PCPS) or SEC Practice Section (SEPS), and can indicate whether any sanctions against firm have been publicly announced).

[90] *See* B AICPA PROFESSIONAL STANDARDS, System of Quality Control for a CPA Firm, QC § 10 (Am. Inst. of Certified Pub. Accountants 1979).

B. The Fiduciary Standard of Care

A fiduciary relation is imposed by law whenever one occupies a position of confidence and trust based upon a high degree of good faith reliance by another upon one's integrity and fidelity.[91] In most engagements, except audit,[92] the CPA is held to be a fiduciary. Certified public accountants giving investment advice owe a fiduciary duty to the client that can shift the burden of proof to the CPA. In a California case, accountants giving investment advice were held liable for a fiduciary breach for diverting a client's investment from the intended purpose.[93] In a Texas case, the court held that a CPA violated a fiduciary duty by failing to disclose the conflict of interest and other relevant facts when advising the client to invest in a real estate venture that the CPA controlled.[94]

Courts applying the law of Illinois,[95] Oregon,[96] the District of Columbia,[97] and Texas[98] have held that certified public accountants entrusted with client funds are fiduciaries and as such have the burden of proving their discharge of accountability. A Michigan court held that a CPA violated his fiduciary duty by using confidential client information in establishing a competing business.[99] Likewise, where an accounting firm failed to execute a "Notice of Change" form so that a departing CPA could obtain a lump-sum amount in his AICPA-sponsored insurance account, liability was imposed on the theory that the accounting firm was a fiduciary under ERISA.[100]

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[91] *See supra* notes 57-58 and accompanying text.

[92] Franklin Supply v. Tolman, 454 F.2d 1059, 1065 (9th Cir. 1972). The court's finding that a fiduciary relationship was not created, and arguably precluded, by an audit engagement focused on the nature of such employment.

> Here, PMM was acting more in the capacity of arbitrator or fact finder not for one but for two persons[, both the purchaser and seller of a private corporation]. The duty of PMM was not to act as a fiduciary for Franklin; it was, rather, to act independently, objectively and impartially, and with the skills which it represented to its clients that it possessed, to make accurate determinations of fact.

Id. at 1065.

Similarly, a fiduciary relationship has been deemed non-existent between a promoter seeking "due diligence" information and an accountant, even though the accountant was aware of the intended use of the information. Windon Third Oil & Gas v. FDIC, 805 F.2d 342, 344 (10th Cir. 1986).

For the proposition that no fiduciary duty is owed by the auditor of a company to public investors of the company absent special circumstances, see *Shofstall v. Allied Van Lines, Inc.*, 455 F. Supp. 351, 359-60 (N.D. Ill. 1978)

For a contrary view, see Bloor v. Dansker (*In re* Investors Funding Corp. of N.Y. Sec. Lit.), 523 F. Supp. 533, 542 n.4 (S.D.N.Y. 1980).

[93] En Yun Hsu v. Leaseway Transp. Corp., [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH)¶ 92,043 (March 29, 1985).

[94] Russell v. Campbell, 725 S.W.2d 739, 746-48 (Tex. Ct. App. 1987). A jury returned a verdict for the plaintiffs and the appellate court affirmed treble damages under a Texas act forbidding deceptive trade practices. *Id.* at 747.

[95] Reid v. Silver, 354 F.2d 600 (7th Cir. 1965). The plaintiff, who had engaged in the design and manufacture of "Rose Marie Reid" swimsuits, entrusted over $1.4 million to her CPA for investment purposes. *Id.* at 602, 607. The court held that the financial relationship shifted the burden of proof to the CPA to provide a complete accounting to

A breach of fiduciary duty by the CPA can cause a particular act to fall outside the coverage of his malpractice insurance policy.[101] In a New York case, the court held that allegations that the CPA firm received undisclosed commissions on the sale

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demonstrate compliance with the fiduciary standard of care. *Id.* at 607.

[96] Croisant v. Watrud, 248 Or. 234, 432 P.2d 799, 804 (1967). A CPA placed in charge of collecting the client's revenues and making disbursements was required by the fiduciary relationship to show his discharge of accountability. *Id.*

[97] Cafritz v. Corporation Audit Co., 60 F. Supp. 627 (D.D.C. 1945). The client recovered over $36,000 because the accountant to whom money had been entrusted was unable to meet his burden of establishing performance of his fiduciary duties. *Id.* at 631, 634. "When a fiduciary is under a duty to account and he fails to do so the only inference to be drawn is that he could not satisfactorily explain the transaction without an omission of guilt." *Id.* at 632.

[98] Squyres v. Christian, 242 S.W.2d 786, 790 (Tex. Civ. Ct. App. 1951). The court held that a CPA who had borrowed $7,000 from a client occupied a confidential and fiduciary relationship with his client, and as a result the burden of proof shifted to the CPA to show that the transaction was "as fairly conducted as if between strangers." *Id.* at 791.

[99] Shwayder Chem. Metallurgy Corp. v. Baum, 45 Mich. App. 220, 206 N.W.2d 484, 486-87 (1973). Defendant, a certified public accountant, provided consulting services for the plaintiff in the areas of cost accounting, financial accounting, and operational management. Subsequently Baum was employed by the plaintiff as its business manager; as a condition of employment he signed an agreement of confidentiality and non-competition. *Id.* at 486. The defendant proceeded to form a competing company, prompting the plaintiff to sue for an accounting, damages and injunctive relief. *Id.* Although the court of appeals refrained from granting the whole of the plaintiff's prayer, it did find that Baum "stood in a fiduciary and confidential relationship . . . and breached the duties and obligations arising from that relationship . . . ." *Id.* at 487. *Compare* Agra Enter., Inc. v. Brundozzi, 302 Pa. Super. 166, 448 A.2d 579, 583 (1982)(CPA was not liable for hiring client's employee and setting up competing business).

[100] Blatt v. Marshall & Lassman, 812 F.2d 810, 812-13 (2d Cir. 1987).

[101] *E.g.*, George Muhlstock & Co. v. American Home Assurance Co., 117 A.D.2d 117, 502 N.Y.S.2d 174, 179 (1986).

of tax shelter investments to clients indicated "a conflict of interest in violation of professional guidelines," and that the activity was outside New York's statutory definition of public accountancy; the insurer had no duty to defend a suit brought by a client based on a violation of the federal securities law.[102] In a Florida case, the CPA firm presented two expert witnesses who testified that "practice" or "professional services" included whatever the insured did, including a service performed only a single time.[103] However, on cross-examination, both experts admitted that unauthorized borrowing from a client was not covered under "professional accounting practice."[104]

C. *Higher Standards for the Specialist*

Where the professional claims to be a specialist or undertakes work generally recognized as a specialty, the courts tend to apply the higher standard for specialists.[105] The courts reason that professionals should not be allowed to attract business as specialists and then defend their mistakes as laymen.[106] Similarly, the *Restatement of Trusts*, which originally required a trustee to exercise the care of an ordinary prudent man, now provides that if the trustee procures business by representing greater skill, then he is under a duty to employ the superior skill.[107] Likewise, section 7-302 of the UNIFORM PROBATE CODE provides that if a trustee is named on the basis of representations of special skills or expertise, then he is under a duty to use those skills.[108]

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[102] *George Muhlstock & Co.*, 502 N.Y.S.2d at 179-80. The court stated that the insurance policy language covered only liability for the breach of a duty as an accountant. *Id.* at 179. The court further stated that the accountant had acted as a broker, which was not within the coverage of his policy. *Id.* at 179-80. The court then found that since the case was not within the scope of the policy's coverage there was no duty to defend. *Id.* at 179.

[103] Duke v. Hoch, 468 F.2d 973, 976 (5th Cir. 1972). One expert testified that professional services included whatever that particular insured did in the course of his specific business, as long as it was reasonable for an accountant to do so. *Id.*

[104] *Duke*, 468 F.2d at 976-77. The court concluded that "his practice" included only services related in some way to accountancy, and that this did not include borrowing money from a client without the client's approval. *Id.*

[105] *See* Annotation, *Physicians and Surgeons: Standard of Skill and Care Required of Specialist*, 21 A.L.R.3d 953, 953-54 (1968); *see also supra* note 59.

[106] Coberly v. Superior Court, 231 Cal. App. 2d 685, 689, 42 Cal. Rptr. 64, 67 (1965). A professional trustee holding himself out as a specialist was not allowed to claim exculpatory powers to excuse negligence. *Id.*

[107] RESTATEMENT (SECOND) OF TRUSTS § 174, comment a (1959); *see also* II A. SCOTT

In a malpractice suit against an attorney who was a specialist in maritime law, a California court held that "[a] lawyer holding himself out to the public and the profession as specializing in an area of the law must exercise the skill, prudence, and diligence exercised by other specialists of ordinary skill and capacity specializing in the same field."[109] The court ruled that, except where negligence is clearly established by the facts, expert testimony is required to establish the standard of care.[110] Furthermore, where the claim is related to the specialty, only persons "knowledgeable in the specialty can define the applicable duty of care and opine whether it was met."[111]

Even those professionals who disclaim knowledge in the specialty may be held to the higher standard of care for the specialty when they undertake to perform the task instead of referring to or consulting with a specialist.[112] Thus, even though an attorney stated that he was not a tax specialist, he was held liable for a defective Clifford trust based on a jury instruction adapted from medical malpractice cases.

> It is the duty of an attorney who is a general practitioner to refer his client to a specialist or recommend the assistance

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& W. FRATCHER, THE LAW OF TRUSTS, § 174.1 (4th ed. 1987)(citing cases supporting higher standard of care for corporate, professional trustees).

[108] UNIFORM PROBATE CODE § 7-302 comment (4th ed. 1975).

[109] Wright v. Williams, 47 Cal. App. 3d 802, 810, 121 Cal. Rptr. 194, 199 (1975). The court stated that a lawyer's duty encompassed both a knowledge of the law and an obligation of diligent research, as well as informed judgment. *Id.* at 809, 121 Cal. Rptr. at 199. Furthermore, the court found that the attorneys were required to use the same standard of care as members of the profession in the same or similar locality under similar circumstances. *Id.*

[110] *Id.* at 810-11, 121 Cal. Rptr. at 200. Expert testimony was required where the failure of the attorney's performance was known only to a person knowledgeable in that speciality. *Id.*

[111] *Id.* The court noted, however, that in some circumstances the failure of an attorney's performance was so clear that a trier of fact was allowed to find professional negligence without expert testimony. *Id.* at 810, 121 Cal. Rptr. at 200.

[112] Horne v. Peckham, 97 Cal. App. 3d 404, 414, 158 Cal. Rptr. 714, 720 (1979). The court rejected the contention that an attorney was not required to refer his client to a specialist or to recommend the aid of a specialist to avoid malpractice. *Id.*

> of a specialist if under the circumstances a reasonably careful and skillful practitioner would do so.
>
> If he fails to perform that duty and undertakes to perform professional services without the aid of a specialist, it is his further duty to have the knowledge and skill ordinarily used by specialists in good standing in the same or similar locality and under the same circumstances. A failure to perform any such duty is negligence.[113]

D. National Versus Local Standards

The trend toward national standards was first established by court decisions dealing with specialists.[114] Standards for specialists tend to be nationwide or non-geographic standards, as noted by a number of courts dealing with medical malpractice which have held the specialist to a national standard of care for the specialty.[115] However, national standards are gradually replacing community standards in other situations as well.[116] For example, in *Hall v. Hilburn* the Mississippi Supreme Court embraced national standards of care for general medical practice.[117] In *Hall*, the plaintiffs tendered expert testimony by doctors residing in Cleveland, Ohio, which was originally excluded from evidence under Mississippi's "locality" rule.[118] However, on petition for rehearing, the Mississippi Supreme Court abolished this rule in favor of admitting expert testimony from anywhere within the United States provided that the testimony was based on information reasonably available to the treating physician.[119] Once informed of the local facilities (whether by visitation, listening to other witnesses, or by hypothetical question), national experts may express opinions as to the defendant's compliance with the professional duty.[120]

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[113] *Id.* The court found that an attorney had the duty to refer his client to a tax specialist even though he had informed his client that he was not a tax specialist. *Id.* at 415, 158 Cal. Rptr. at 720. The attorney had the duty to avoid involving his client in unknown areas of the law if research showed an alternative course of action. *Id.* at 415, 158 Cal. Rptr. at 721.

[114] *See* Annotation, *Standard of Care Owed to Patient by Medical Specialist as Determined by Local, "Like Community," State, National, or Other Standards*, 18 A.L.R. 4th 603, 607 (1982).

[115] *Id.* at 614-20.

[116] *E.g.*, Kellos v. Sawilowsky, 254 Ga. 4, 325 S.E.2d 757, 758 (1985). The court found that there was no difference between the Georgia standard and the national standard of care for law practice. *Id.*

[117] Hall v. Hilburn, 466 So. 2d 856, 870 (Miss. 1985). The court stated that state lines are irrelevant because medical centers of adjoining states were a real part of medical care in Mississippi. *Id. See generally* Causey, *Mississippi Adopts National Medical Standards for Measurement of Medical Malpractice*, 27 J. MISS. ST. MED. A. 68, 68-69 (analytical discussion of Hall v. Hilburn).

[118] *Hall*, 466 So. 2d at 863-64.

Court decisions dealing with accountants have established the rule that expert testimony is generally required in order to avoid dismissal.[121] The expert testimony presented usually deals with AICPA, FASB or SEC rules, thus there is no difference in local and national standards. In one California case, though, the court dismissed a suit against a CPA based on expert testimony that the local practice in San Francisco was to assume that corporate payors of income properly designate the taxable status of moneys reported on IRS Form W-2. However, there was no offer of expert testimony to the contrary.[122] The failure to file a tax return on time has been held to be a breach of the standard of care as a matter of law without reference to expert testimony.[123]

E. Probative Effect of Expert Testimony

1. Judicial Rejection of the Professional Standard

The courts generally reserve the right to question or reject the professional standard established by the expert testimony and hold the defendant to a higher standard of care.[124] While

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[119] *Id.* at 874-75. The court stated that there was no valid basis to require expert witnesses to be from a certain geographic area to be competent to testify. *Id.* at 874.

[120] *Id.* at 875.

[121] Kemmerlin v. Wingate, 274 S.C. 62, 261 S.E.2d 50, 51 (1979). A client's suit against an accounting firm was dismissed because there was an absence of expert testimony establishing the standard of care. *Id.*

[122] Lindner v. Barlow, Davis & Wood, 210 Cal. App. 2d 660, 27 Cal. Rptr. 101 (1963).

[123] Sorenson v. Fio Rito, 90 Ill. App. 3d 368, 413 N.E.2d 47, 53 (1980). The failure to file a tax return constituted negligence so explicit that expert testimony concerning the standard of care was not required. *Id.*

[124] As stated by Judge Learned Hand:

> [I]n most cases reasonable prudence is in fact common prudence; but strictly it is never its measure; a whole calling may have unduly lagged in the adoption of new and available devices. It may never set its own tests, however persuasive be its usages. Courts must in the end say what is required; there are precau-

the medical profession has traditionally been exempt from such judicial scrutiny, the courts now indicate a willingness to reject medical standards that fail to afford essential protection that is available at modest or nominal cost.[125] Court decisions rejecting the professional standard in the accounting community have been rare, but a lower court in one case appeared to reject the professional standards for accounting for real estate sales as it stated:

> Much has been said by the parties about generally accepted accounting principles and the proper way for an accountant to report real estate transactions. We think this misses the point. Our inquiry is properly focused not on whether Laventhol's report satisfies esoteric accounting norms, . . . but whether the report fairly presents the true financial position . . . to the untutored eye of an ordinary investor.[126]

> tions so imperative that even their universal disregard will not excuse their omission.

The T.S. Hooper, 60 F.2d 737, 740 (2d Cir. 1932).

In Texas & Pacific Railway v. Behymer, 189 U.S. 468, 469-70 (1903), the plaintiff (train brakeman) obeyed orders to get on top of train cars covered with ice and let the brakes off. *Id.* at 469. The engine then picked up the train cars and stopped suddenly, which upset plaintiff's balance so that he caught the bottom of his trousers on a projecting nail and was thrown between the cars. *Id.* The United States Supreme Court rejected the argument that liability depended on "whether the freight train was handled in the usual way" and held that "this exception needs no discussion. The charge embodied one of the commonplaces of law. What is usually done may be evidence of what ought to be done, but what ought to be done is fixed by a standard of reasonable prudence, whether it is complied with or not." *Id.* at 470; *see also* The T.J. Hooper, 60 F.2d 737, 739-40 (2d Cir. 1932)(tugboat not equipped with radio set to receive storm warnings held unseaworthy); Marsh Wood Prod. Co. v. Babcock & Wilcox Co., 207 Wis. 209, 240 N.W. 392, 396-97 (1932)(failure to test steel used in boiler negligent despite contrary custom of manufacturers). *See generally* Morris, *Custom and Negligence*, 42 COLUM. L. REV. 1147 (1942).

[125] In Helling v. Carey, 83 Wash. 2d 514, 519 P.2d 981, 982-83 (1974), ophthalmologists were held liable for blindness of a thirty-two-year-old woman despite undisputed medical testimony that customary practice did not include glaucoma tests for patients under forty because only one out of twenty-five thousand persons under forty contracts the disease. *Id. See generally*, Note, *Physicians and Surgeons — Standard of Care — Medical Specialist May be Found Negligent as Matter of Law Despite Compliance with the Customary Practice of the Specialty*, 28 VAND. L. REV. 441, 441-53 (1975)(analysis of *Helling*).

[126] Herzfeld v. Laventhol, Kerkstein, Horwath & Horwath, 378 F. Supp. 112, 121 (S.D.N.Y. 1974).

However, the appellate court affirmed the liability of accountants based on the accountants' violation of professional standards dealing with realization of revenue, audit evidence and disclosure.[127]

In a case involving a criminal conviction of a CPA, the AICPA filed an amicus brief which argued that the court failed to make a distinction between the duty of an accountant with respect to audited versus unaudited financial statements.[128] Without rejecting the professional standards, the court found that the distinction was not relevant to the particular factual setting, stating that "[t]he issue on this appeal is not what an auditor is generally under a duty to do with respect to an unaudited statement, but what these defendants had a duty to do in these unusual and highly suspicious circumstances."[129]

In a case involving the collapsed sports car production venture of auto magnate John DeLorean, the United States Court of Appeals for the Eleventh Circuit established its own standard, without the benefit of expert testimony, and held that an accountant can be liable for failure to warn investors of fraud despite the fact that all outstanding auditors' reports were accurate as of their issuance dates.[130] While the court acknowledged that prior cases had limited the duty to disclose information discovered after completion of a report of information indicating the report was inaccurate as of its date of issue, the court reasoned that "the cost to the accountant of revealing the information [is] minimal, and the cost to investors of the information remaining secret [is] potentially enormous."[131]

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[127] Herzfeld v. Laventhol, Kerkstein, Horwath & Horwath, 540 F.2d 27, 35-37 (2d Cir. 1976); *see* Note, *Herzfeld Revisited After Hochfelder: The "Scienter" Standard Applied to the Reporting of Uncertainties*, AM. BUS. L.J. 252, 259-67 (1976)(discussing application of accounting standards to facts in *Herzfeld*).

[128] United States v. Natelli, 527 F.2d 311, 323 (2d Cir. 1975), *cert. denied*, 425 U.S. 934 (1976). Defendant, affiliated with Peat, Marwick, Mitchell & Co., was convicted of criminal violations of the Securities Exchange Act of 1934 on charges of creating "materially unaudited statement of earnings for inclusion in a proxy statement issued by National Student Marketing. *Id.* at 314-15.

[129] *Id.* at 323. The court noted that the defendant was aware of the highly suspicious nature of the figures incorporated in the nine-month statement, and distinguished this case from one where an auditor "would not be chargeable simply because he failed to discover the invalidity of booked accounts receivable, inasmuch as he had not undertaken an audit with verification." *Id.* at 320.

[130] Rudolph v. Arthur Anderson & Co., 800 F.2d 1040, 1043-47 (11th Cir.), *cert. denied*, 107 S. Ct. 1604 (1986).

2. Nonconclusive Effect of the Professional Standard

In a leading case upholding the criminal conviction of certified public accountants, following overwhelming expert testimony as to compliance with generally accepted accounting principles, the court said:

> The "critical test" was whether the financial statements as a whole "fairly presented the financial position of Continental as of September 30, 1962, and whether it accurately reported the operations for fiscal 1962." If they did not, the basic issue became whether the defendants acted in good faith. Proof of compliance with generally accepted standards was "evidence which may be very persuasive but not necessarily conclusive that he acted in good faith, and that the facts as certified were not materially false or misleading".[132]

In connection with the criminal conviction of three auditors of Equity Funding Corporation, the Court of Appeals for the Ninth Circuit upheld jury instructions that deviation from GAAP or GAAS was evidence, but not necessarily conclusive evidence, that the defendants did not act honestly and that the financials were false and misleading.[133] In another Ninth Circuit case dealing with federal and common law claims, the court held that compliance with "generally accepted accounting standards" is not a defense when the accountant fails to disclose known material facts.[134] One district court has held that financials cannot be fraudulent where the accounting methods prevail in the industry and conform with generally accepted accounting procedures endorsed by the accounting profession as a whole.[135]

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[131] *Rudolph*, 800 F.2d at 1044.

[132] United States v. Simon, 425 F.2d 796, 805-06 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970).

[133] United States v. Weiner, 578 F.2d 757, 786-87 (9th Cir. 1978), *cert. denied*, 439 U.S. 981 (1979).

[134] SEC v. Seaboard Corp., 677 F.2d 1301, 1312-13 (9th Cir. 1982). The court recognized the protection normally afforded accountants through adherence to generally accepted accounting standards, but relying upon United States v. Simon, "assumed" that such standards do not provide protection from liability when the accountant fails to reveal material facts which he knows should be revealed. *Seaboard Corp.*, 677 F.2d at 1313 n.15.

F. Breach of the Defendant's Standards

Some courts have looked to the defendant's own standards in establishing the standard of care and the deviation from it.[136] The basis for doing so is apparently the theory that the defendant's standards are admissions of a party.[137] The problem which is not addressed in these cases is that the defendant's standards may be higher than the standard required in the particular situation. In *Robert Wooler Co. v. Fidelity Bank*,[138] the court supported the testimony of plaintiff's experts as to the duty to warn of internal control weaknesses in a nonaudit engagement by looking to the defendant's checklist for the engagement.[139] In *Escott v. BarChris Construction Corp.*,[140] the court adopted the defendant's audit program as representative of the professional standard, and said, "Accountants should not be held to a higher standard than that recognized in their profession. I do not do so here . . . . He did not take some of the steps which Peat, Marwick's written program prescribed."[141]

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[135] Shahmoon v. General Dev. Corp., [1973-1974 Transfer Binder] Fed. Sec. L. Rep. (CCH)¶ 94,308 at 95,039 (S.D.N.Y. Dec. 1, 1973).

[136] *E.g.*, Jenson v. Touche Ross & Co., 335 N.W.2d 720, 726-27 (Minn. 1983).

[137] *Id.* at 727. In *Jensen*, purchasers of bulk silver from a defunct company sued the auditors, alleging that Touche Ross was liable under several theories for failure to disclose that its client was being investigated by the SEC and by state securities commissions. *Id.* at 723-24. Resolution of the dispute required consideration of several evidentiary issues; specifically evidence of how another firm conducted an audit of a similar operation was deemed inadmissible as to the defendant's standard of care, and internal auditing guidelines and manuals for conducting an audit were deemed admissible as party admissions. *Id.* at 726-27.

[138] 330 Pa. Super. 523, 479 A.2d 1027 (1984).

[139] *Robert Wooler Co.*, 479 A.2d at 1033. The court found that the checklists reminded the accountant's employees to be aware of potential theft in the internal bookkeeping department. *Id.* The expert witnesses testified that when performing unaudited services for a corporation, an accountant possessing reasonable accounting skills would have recognized the potential for theft within the corporation. *Id.*

[140] 283 F. Supp. 643 (S.D.N.Y. 1968).

[141] *Escott*, 283 F. Supp. at 703.

IV. ISSUES PRESENTED BY THE *Touche Ross* DECISION

Analysis of the Mississippi Supreme Court's decision in *Touche Ross & Co. v. Commercial Union Insurance Co.*[142] reveals these issues:

- Was the plaintiff bonding company a third party or a successor to claims of the client, Fidelity Bank?
- Should an accountant's duty of due care extent to all "who request and receive a financial statement from the audited entity?"[143]

These issues are explored below after a brief summary of the case.

A. *The Facts and Holdings*

Touche Ross & Co. issued its audit report on the 1977 financial statements of Fidelity Bank, and USF&G, upon seeing the audit report, cancelled its insurance that protected Fidelity Bank against employee fraud.[144] Commercial Union Insurance Company then issued its replacement policy, and later sued Touche Ross for negligence alleging that its reliance on the Touche Ross audit caused its loss of the $1 million policy limits which the FDIC required it to pay.[145] The FDIC attributed the bank's failure to "fraudulent and dishonest activities" that commenced four months *after* Touche Ross had completed its audit.[146] The jury found Touche Ross negligent, and awarded Commercial Union one million dollars in actual damages and five hundred thousand dollars in punitive damages.[147] When deciding the case, the Mississippi Supreme Court stated that the issues were:

- "Is an independent auditor liable to a third party, who, though lacking privity, relies to his detriment on financial statements negligently prepared?"[148]

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[142] 514 So. 2d 315 (Miss. 1987).

[143] *Id.* at 322.

[144] *Id.* at 321.

[145] *Id.* at 315-16.

[146] *Id.* at 323.

[147] *Id.* at 315.

[148] *Id.* at 318.

- "Is an independent auditor liable to a third party, when losses occur through criminal conduct, wholly subsequent to performance of the audit?"[149]

The court answered its first question in the affirmative, holding that an auditor has a duty of due care to all "who request, and receive a financial statement from the audited entity for a proper business purpose, and who then detrimentally rely on the financial statement, suffering a loss proximately caused by the auditor's negligence."[150] The court answered the second question in the negative, ruling that one who is negligent may be liable for damages from reasonably anticipated intervening events, but that subsequent criminal acts are only remote possibilities and as such are not within the responsibility of a negligent auditor.[151]

B. *The Relationship of the Parties*

Why the court framed the issues in terms of an auditor's liability to a third party is not clear. It is well settled that whenever an insurer pays an embezzlement loss, the insurer becomes subrogated to any right of action that the insured had against the auditor.[152] Similarly, the FDIC (Federal Deposit Insurance Corporation),[153] FSLIC (Federal Savings and Loan Insurance

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[149] *Id.* at 323.

[150] *Id.* at 322.

[151] *Id.* at 324.

[152] National Sur. Corp. v. Heinbokel, 154 F.2d 266, 267 (3d Cir. 1946)(applying Pennsylvania Law in diversity case, plaintiff sued as subrogee auditors who allegedly failed to discover theft of securities); Maryland Casualty Co. v. Cook, 35 F. Supp. 160, 164 (E.D. Mich. 1940)(court held negligent auditor liable for embezzlement losses); Dantzler Lumber & Export Co. v. Columbia Casualty Co., 115 Fla. 541, 156 So. 116, 118-20 (1934)(insurer was subrogated to client's rights and gist of action for auditor's failure to discover embezzlement was in tort); Owyhee County v. Rife, 100 Idaho 91, 593 P.2d 995, 997 (1979)(bonding companies claiming subrogation joined with client who sought to recoup uninsured balance of losses); Western Sur. Co. v. Loy, 3 Kan. App. 2d 310, 594 P.2d 257, (1979)(bonding company not required to prove fraud or gross negligence); National Sur. Corp. v. Lybrand, 256 A.D. 226, 9 N.Y.S.2d 554, 556 (App. Div. 1939)(after paying embezzlement loss, bonding company sued as assignee of client). *Compare* American Indem. Co. v. Ernst & Ernst, 106 S.W.2d 763, 765 (Tex. Civ. App. 1937)(court treated surety as third party required to prove fraud).

[153] *See* Landy v. FDIC, 486 F.2d 139, 149 (3rd Cir. 1973), *cert. denied*, 416 U.S. 960 (1974)(FDIC was both subrogee and receiver in bankruptcy).

Corporation), and SIPC (Securities Investor Protection Corporation) are subrogated to any right of action that the insured has against a negligent auditor. The doctrine of subrogation is well established by numerous precedents in Mississippi.[154] Thus Commercial Union, as subrogee, was successor to rights of Fidelity Bank and was owed a duty of due care by Touche Ross. Touche Ross could assert the same defenses against Commercial Union that it could assert against Fidelity Bank. Perhaps the court's third-party treatment was dictated by the theory and evidence presented in plaintiff's case. If the theory and evidence was limited to recovery for its insuring decision, as opposed to recovery for the auditor's failure to detect and reveal control weaknesses, the plaintiff thus failed to present a claim as subrogee.[155]

C. *Scope of the Accountant's Duty*

The Mississippi Supreme Court noted the Mississippi statutory provision that removes privity as a requirement in all actions for economic loss brought on account of negligence.[156] However, the court could have simply construed this statute as a codification of the common-law rule as expressed in the *Restatement (Second) of Torts* which limits the scope of duty to "a limited group of persons for whose benefit and guidance he intends to supply the information."[157] Instead, the court adopted the New Jersey rule and extended liability for negligence to all recipients of a "financial statement from the audited entity"[158] and said, "Of course, the auditor remains free to limit the dissemination of his opinion through a separate agreement with the audited entity."[159] Unfortunately, most auditors find it impracticable to explain to clients why audit reports cannot be freely distributed or to use such a device in risk management. Financial analysts in Mississippi will insist upon receiving reports directly from the audited entities to assure their protected status.

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[154] *E.g.*, Kimberly-Clark Corp. v. Alpha Bldg. Co., 591 F. Supp. 198 (N.D. Miss. 1984)(surety has equitable right of subrogation to indemnity for all losses by virtue of having given its bond); Travelers Indemn. Co. v. Clark, 254 So. 2d 741, 745-46 (Miss. 1971)(rights of surety to subrogation for its loss founded on equitable principles independent of contractual rights based on bond).

[155] Similarly, the court in Pahre v. Auditor of State of Iowa, 422 N.W.2d 178 (Iowa 1988), failed to discuss a guaranty company's claim as subrogee and relied on the RESTATEMENT in dismissing third-party claim.

[156] *Touche Ross*, 514 So. 2d at 321.

[157] *See supra* note 6.

[158] *Touche Ross*, 514 So. 2d at 322.

D. Reliance

The third party should be required to prove reliance upon the entire report including any qualifications in the auditor's opinion and any explanatory footnotes included in the statements. Under recently revised reporting standards, the audit report explains (1) inconsistency, (2) uncertainty, and (3) going concern questions, by an audit report reference to explanatory footnotes.[160] The Mississippi court made a distinction without a difference by its focus on the source of the report from the audited entity instead of requiring reliance upon the *entire* report including these important footnotes. In *Raritan River Steel v. Cherry, Bekaert & Holland*,[161] the North Carolina Supreme Court dismissed the suit of a third party that alleged reliance upon a Dun and Bradstreet, Inc. report and held the plaintiff must prove reliance upon the entire auditor's report.

E. Public Policy

Mississippi CPAs may be astonished by the Mississippi Supreme Court's approval of the California view that "[t]he risk of loss is more appropriately placed on the accounting profession which is better able to pass such risk to its customers and the ultimate consuming public."[162] Heretofore, the CPA has never attempted to provide insurance as to financial statements any more than doctors who never insure that patients will be cured or that operations will be successful, nor more than lawyers who never insure that cases will be won or that wills or contracts will effectuate their desired purposes. The role of insurance is not the same as the exercise of due care for the benefit of a limited group. Thus one court, analyzing reasonable expectations from professional persons, said, "Those who hire such persons . . . purchase service, not insurance."[163] The New Jersey and California views have now been repudiated by legislatures in Arkansas,[164] Kansas,[165] and Illinois,[166] and by courts in Florida,[167] Georgia,[168] Indiana,[169] New York,[170] and North Carolina.[171]

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[159] *Id.* at 323.

[160] *See* Guy and Sullivan, *The Expecation Gap Auditing Standards*, J. Account., April 1988, at 43.

[161] 322 N.C. 200, 367 S.E.2d 609, 612-13 (1988).

[162] *Touche Ross*, 514 So. 2d at 322 (quoting International Mortgage Co. v. John P. Butler Accountancy Corp., 177 Cal. App. 3d 806, 820, 223 Cal. Rptr. 218, 227 (1986)).

The Mississippi Supreme Court's ruling comes at a time when the insurance industry in general and professional liability insurance in particular is recovering from a crisis. Insurance premiums for CPAs have increased by a factor of five since 1984 while deductibles have increased many times over. One out of five CPA firms responding to a recent survey indicated that it had been forced to drop its insurance coverage.[172] Several legislatures, including Mississippi, have made changes or are considering changes in their respective civil justice systems to limit the scope of civil liabilities.[173]

V. A PROPOSAL

A. *Scope of Duty*

The broad spectrum of views as to the scope of the accountant's duty to use due care is clearly undesirable in an area involving such a compelling public interest. The accountant is not able to anticipate the risk/responsibility in some jurisdictions, while in other situations the activities may involve several jurisdictions with uncertainty as to the applicable law. The effect of the uncertainty and spectrum of approaches is that liberal jurisdictions provide third parties with a windfall that they never bargained for in any contractual relationship. The result is a distortion in the loss ratios for these jurisdictions and consequent disorder for accountants' insurance. The final result of the diversity may serve to diminish recoveries in the liberal jurisdictions due to an increasing trend of accounting firms to go without insurance coverage, either because they cannot obtain it, or because coverage cannot be obtained at a reasonable cost.

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[163] Delmar Vineyard v. Timmons, 486 S.W.2d 914 (Tenn. Ct. App. 1972)(auditor held not liable despite omission of payables and overstatement of inventory).

[164] *See supra* note 21 and accompanying text.

[165] *See supra* note 22 and accompanying text.

[166] *See supra* note 20 and accompanying text.

[167] *See supra* note 9.

[168] *See supra* note 32.

[169] *See supra* note 10.

[170] *See supra* note 11.

[171] *See supra* notes 38, 161 and accompanying text.

[172] *As Accounting Firms Premiums Soar, Some Might Drop Liability Insurance*, Wall Street Journal, May 30, 1985 at 17, col. 1.

[173] Mednick, *Accountant's Liability: Coping with Stampede to the Courtroom*, J. Account, Sept. 1987, at 118, 122.

The subject of professional responsibility for accounting malpractice is one uniquely unsuited to resolution by courts relying upon common law tort theories. The attempts to do so often result in attributing to the role of the accountant much greater responsibility than the accounting industry has ever attempted to undertake. Contemporary auditing standards simply do not result in a guarantee of accuracy of financial reports. While stricter auditing standards can provide greater assurance at a greater cost, it will not be possible for accountants to insure the results of their work any more than a physician can insure the results of surgery, nor more than a lawyer can insure the outcome of a lawsuit. Management has the inherent power to override the tightest controls and deceive the auditor. There will often be no evidence in the client's books which will alert the auditors to a transaction or event. The auditors' ability to verify from outside sources can hardly be exhaustive. In fact, the auditors' efforts have been impeded by the lawyers' tradition of protecting his clients' secrets. Consider for example the situation where an attorney was held to have no duty to disclose his client's insolvency in response to an audit inquiry letter, yet the auditor could be held liable for failure to detect and reveal the client's financial problems.[174]

In view of the complexity of the issues surrounding the role of the accounting industry and the lack of understanding of limitations on its functions, the matter of accountants' professional liability should be addressed by the legislature of each state. Until that can be accomplished, the courts should return to limiting the scope of the accountant's duty, not to strict privity, but to contractual principles as expressed in the recent decision of the Eleventh Circuit interpreting Florida law in a diversity case.[175] The court rejected the test of foreseeability of the third party's reliance and held the proper test was the existence of a contractual relationship between the parties. This contractual relationship exists, the court found, when the accountant performs an audit for the benefit of known third parties. The plaintiff had issued a performance bond for a contractor who went bankrupt. The bonding company sued the contractor's auditor and the case went to trial on the third-party beneficiary theory. The jury found that, although plaintiff was a third-party beneficiary, the accounting firm had not breached its contract by failing to perform with due care. On appeal, the court affirmed that the third party stands in the shoes of the client and is limited to the two-year limitation period for contract claims (as opposed to the four-year period for tort claims) and that any defenses available against the client were also available against the third-party beneficiary.[176]

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[174] Tew v. Arky, Freed, Stearns, Watson, Greer, Weaver & Harris, P.A., 655 F. Supp. 1571, 1572-73 (S.D. Fla. 1987)(on appeal to Court of Appeals for Eleventh Circuit).

Until the legislatures act, the Florida approach, as interpreted by the Eleventh Circuit, will provide a reasonable resolution of the policy issue. Eighty percent of all suits against accountants are by clients who are already protected.[177] The above view brings even more persons under the client's cloak of protection while avoiding placing third parties in a position superior to that of a contracting party. By restricting the duty to contractual principles, the law will then conform to the objective that "the risks reasonably to be perceived defines the duty to be obeyed."[178]

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[175] Seaboard Surety Co. v. Garrison, Webb & Stanaland, P.A., 823 F.2d 434 (11th Cir. 1987).

[176] *Seaboard Sur. Co.*, 823 F.2d at 435-38.

[177] Leibensperger, *8 Steps to Avoid Liability*, CPA NEWSL. Feb. 1987, at 4.

[178] Palsgraf v. Long Island R.R., 248 N.Y. 339, 162 N.E. 99, 100 (1928).

NEVILLE PATTERSON

*James L. Robertson**

A Remembrance**

He called me "Judge" before I was one and so said more of him than of me. I called him "Chief". It was the only name that fit. He looked like a chief justice. In the three and a half years I served with Neville Patterson I marveled at his equal respect and concern for each of his fellow Justices, none of whom are likely to inherit the earth. He made me feel that I was the most important person here. I liked that. I liked him more when I saw he made others feel the same.

But all was not sweetness and light. He was a fierce and tenacious adversary and once his mind was set, it was in concrete. In the tough cases I voted with him more often than not. Still, I recall times when we locked horns, when I thought he had taken leave of his senses. Integrity marked each vote he cast. With so many cases to be considered and voted upon in a day or a week, one cannot help but think politically. Trading votes it's called. If I vote to affirm Smith v. Doe, Justice X's cause of the moment, then he may be more likely to vote with me on Jones v. State this afternoon, or so the idea goes. The Chief was too shrewd a politician not to have been aware. At times I could not understand *why* he thought he was right or *how* he could think he was right, but I never doubted *that* he thought he was right. He set the standard.

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* B.A., University of Mississippi 1962; J.D., Harvard Law School 1965; Justice, Mississippi Supreme Court 1983-present.

** Editor's Note - Neville Patterson died on July 15, 1987, ending forty years of service to the Mississippi judiciary. From 1947 through 1963 he presided as Chancellor for the Thirteenth Chancery District. With the advent of 1964 he became Justice Patterson, and on August 1, 1977, was elevated to the position of Chief Justice of the Supreme Court of Mississippi.

Memorials and retrospectives are frequently marred by the tendency to limit the measure of the man to his obvious achievements, and by the temptation to whitewash personal foibles. Justice Robertson has avoided these pitfalls in his remembrance of Neville Patterson, and in the brief pages that follow recounts his observations of the whole man; in doing so he has afforded us a clue as to the composite genius of Justice Patterson.

That first day, he told me a bit of my colleagues to be. He spoke only good. Then he said, "You'll find that I am the most liberal judge on this Court." I later learned that he said the same thing to other incoming justices. I was slow to understand. He found the teachings of the Warren Court congenial. His opinions reflect an acceptance of constitutional doctrine at a time when others evaded and avoided. But he meant more than that. He thought rights were to be taken seriously. He recounted for me once a debate in en banc conference on a criminal case in which one justice argued, "If we do this, it will make it too hard to convict these criminals," to which another justice replied, "It is supposed to be hard." The Chief thought so, too. He thought a man charged with a crime had a right to walk into the courtroom, back up to the Constitution, and say, "Prove it." His heart told him that was good, for, beneath it all, he knew that law was about people. He was on the side of the little man, the underdog, the widow, the accused felon, the injured worker, the fellow who never had a real chance at life, and the one who had gotten a tough break.

For years he suffered in silence, at least insofar as the outside world knew — and its only means of knowing were the pages of the Southern Reporter. He *was* a liberal in a time when many thought liberals lepers. Of course, I learned that in conference, behind closed doors, he was anything but silent. His last years on the Court brought winds of change. More than twice or thrice, the newer and younger justices would quickly put four votes on the table. (In en banc conference the justices were called upon to announce their votes in inverse order of seniority.) I imagined a chuckle within him when that fourth vote was cast. He could hardly wait for the vote to swing around the table. He would cast the fifth and deciding vote, and then, masking delight, give his reasons, calmly, succinctly and professionally. He had a nice touch.

Privately, he called us upstarts "the yellowjacket court" and left no doubt that he was one of us. Still, he would show respect and deference for those with whom he disagreed. There was no insincerity in either view. Unambiguous lives are scarcely worth knowing — or living. He would go out of his way to solicit the views of those he knew would fight him. He took seriously the principal that one should have an open mind to the point of suppressing one's instincts. Over coffee or a drink afterwards, when one of us would become a bit exuberant, he would remind us that judges don't "win" cases and find a way to say something positive or understanding about those who voted the other way.

Neville Patterson's success as Chief Justice was considerable. This is downright remarkable, since the office comes with few of the trappings and powers customarily thought a part of it. The senior Justice is the Chief Justice. As he once told me, "I didn't get to be Chief Justice by being real smart. I just outlived those other bastards," and of his authority he would say, "I've got one vote just like everyone else and nothing beyond my powers of persuasion." But those powers were considerable because of who he was and what he was. He had the right stuff.

The grand achievements are familiar. Reclaiming the rule-making powers for the judiciary and evicting the legislature from the executive department of state government — these are the twin towers of his Chief Justiceship, permanent monuments on the landscape of our society.

He had no real interest in rules of procedure. His concern was the integrity of the judiciary. He dreamed of a judicial department of government truly separate from and equal to the legislative and the executive. He wanted the judiciary, historically and the stepchild of Mississippi government, to assume its rightful role. His prejudice was that the judiciary had a greater impact upon the lives of people than any other branch of government. And so, in *Newell v. State*, 308 So.2d 71 (Miss. 1975), he fashioned and cajoled the Court into a unanimous assertion of the rule-making power. Six years later and after several false starts, he and others gave us the Mississippi Rules of Civil Procedure. I don't know which had more to do with the outcome of that blood letting: his backbone or his bullheadedness, yet in those times he proved the pragmatist as well. When asked why he gave in to the excision of Rules 4 and 14 — a step many rule watchers found wholly inexplicable — his answer was simply put: "It was necessary to keep that fifth vote." Saving the Rules was more important than saving any particular rule. Indeed, as the months and years went on, more than one or two Rules cases came to the Court and made it apparent that he didn't really know much of what was in the Rules. "Is that in those Rules?" he would ask me. He even wrote opinions on points covered by the Rules without mentioning them and deciding the point incorrectly. No matter. Neville Patterson saw forests, not trees.

He saw the key to permanency: establishing an Advisory Committee on Rules, a committee appointed by the Court fairly representative of the bench and bar but wholly independent of control by anyone other than the Court. He went about the task quietly. It was the cornerstone of his grand design, a point about which he had the sense to say little. His antennae detected a broad consensus supporting rules of evidence patterned after the Federal Rules of Evidence. He persuaded the Court to establish the Rules Committee and then saw that its first task was the Rules of Evidence. Success on so massive a project would secure the victory. It was a conscious plan, and it worked. But, even then, there was a moment that showed the measure of the man. The public record reflects that the Rules of Evidence were adopted by Order of September 24, 1985. There were six votes to adopt the Rules five months earlier. Two members of the Court, however, expressed sincere concerns. The Chief had the prescience to see that unanimity was vital and the patience to persevere until unanimity was achieved. He was right. Once January 1, 1986, came and passed, one had the sense that he considered his work complete. True, there were projects yet on the drawing board, his proposal for an intermediate court of appeals most notable. Early in 1986, he told us he would not be a candidate for re-election. He began talking of retirement.

But I have not told all of the story. There is the other tower: *Alexander v. Allain* back in 1983.

He didn't just take that case for himself. The Chief Justice in Mississippi has no such authority. He came to write *Alexander* the same way each other case is assigned. He drew it. More accurately, on a day when he was absent, the rest of the Justices conducted a drawing; I drew for the Chief and got the slip with the "X" on it. It was fitting that he write *Alexander*, as it was that Earl Warren write *Brown v. Board of Education.*

He perceptively labeled it the "Separation of Powers Case." As I preached the tyranny of labels, he saw their power. What a case is called can say much of how it will be perceived and may influence how it is decided. One might have ambivalent feelings about Bill Allain's war with the Legislature, but how could an American lawyer be against separation of powers? He kept it on that plane.

His shrewdness didn't end there. Timing was everything. He had a sixth sense about it. "It's all in knowing when the fish are biting, when a woman's in the mood, and when to bring a case to a vote," he once told me.

He held the case for months. Together with his law clerk, he studied it almost to the exclusion of all else. I was check judge on the case and was privileged to watch him work. He gradually moved around the different offices on the Court mentioning one point to Justice X, another to Justice Y. He would tell a few of his ideas at coffee in the morning. Slowly he built a consensus, saying what he thought, soliciting comments and critique. But nobody saw a word on paper. His touch was masterful. After hours, days and weeks of drafting, editing, writing and rewriting, he put a draft opinion on everyone's desk and placed the matter on the agenda for en banc conference four days later. He gave everyone just enough advance notice of his thinking but not too much. In conference his tone was reasonable, soliciting, conciliatory. Different justices suggested ideas for changes in wording. These he accepted with good grace and many were incorporated into the final draft. Between unanimity and perfection, there was no doubt which he preferred. It mattered not so much what the opinion said as how it would be read. He knew that nothing would contribute more to how it was read than a nine to nothing vote. At the end of the day, unanimity had been achieved. He asked and secured leave to circumvent the normal procedure of formal circulation of an opinion one week before release. All agreed that it would be handed down on Wednesday. The next day, Tuesday, he held his breath. At least one Justice that I know of proposed several additional changes in wording. He quickly acceded. They would never be noticed and he knew it. The opinion was released at 9:30 Wednesday morning, November 23, 1983, and the rest is history.

There were the victories in which he played a supporting role — property tax equalization and the abolition of sovereign immunity — and the causes lost — the Judicial Council. Through it all, he was proud of his Court, almost as a father. He told me our Court was better than the Fifth Circuit. I was never sure whether he believed it. I knew he wished it desperately.

What sort of man was he? There were certainly others who knew him better than I, longer than I. He was complex, at times a contradiction, at others a conniver. There was method and professionalism in his madness.

He had his list of the state's SOBs and knew he was on others' lists. He would have been disappointed had he thought he wasn't on several. I remember the law clerk he reduced to tears and one who thought him pigheaded, though she adored him. Several secretaries to other Justices did not like him, thought him mean. His last loved him. I knew lawyers who thought him arrogant, cold. Many more saw him warm and compassionate.

It is the fate of man that his best qualities inspire adoration in some and at once contempt in others. Nor do we agree which qualities are his best. Our eulogies strip him of his humanity when they deny the ambiguities in his life. He becomes a saintly- and banal-bore.

At the coffee table or over drinks he was a delightful companion. His fishing yarns and tales of the old days in Lawrence County were a joy. He had an earthy and infectious sense of humor. I regret that many members of the bar never saw that side of him. All too many lawyers knew him only for the state of the judiciary addresses he would give at the annual Bar Convention. He would get up and read his speeches, tediously so, filling them with statistics and putting everybody to sleep. I sensed that he was never comfortable in that setting.

I remember the time during oral argument when a young lawyer was struggling valiantly but in vain to make a point and finally in desperation said "Well, Your Honors, when I was in law school they taught me . . . ." He was interrupted by another Justice's "Counsel, I've been trying for twenty-five years to forget all that stuff they taught me in law school," to which the Chief quickly quipped "And you've damn well succeeded, too."

Then there was *City of Clinton v. Smith*, the Clinton beer ordinance case, in which the legality of a local option beer referendum was at issue. At the end of the argument, the Chief made the customary formal announcement that the Court would be in recess until the next morning and, as we left the bench, he said to me in a voice that I suspect could be heard in the courtroom, "I should have said 'The Court will be in recess for a cold beer.' "

There was in him a genuine streak of the gentleman, old fashioned, Southern style. I noticed it in the way he courted Lenore Prather. He was ever solicitous. More than with the other Justices, he went the extra mile to make her feel a Justice. But he could never forget she was a woman. Once en banc, one judge told a particularly off-color joke, as only he can. Everyone turned red and roared including Lenore, but not the Chief. Later he called that judge to his office and asked him not to do that again when Justice Prather was present. The surprised judge quickly responded, "Lenore laughed as hard as anyone. She wasn't embarrassed." "I know that," the Chief replied, "but I was embarrassed." He genuinely was.

To have been so progressive in so many areas — as a matter of instinct more than intellect — he still had many old-fashioned attitudes. He never quite accepted my constant questioning of lawyers from the bench during oral argument. Most of my appellate experience as a lawyer had been before the Fifth Circuit. I had come to expect constant questions. I thought (and think) a panel is supposed to be "a hot court." But the Chief had a different view. He thought a lawyer was entitled to make his argument without interruption, as was a preacher in his pulpit. He would be almost apologetic when he would ask a question. Once he blatantly apologized to a lawyer for my constant interruptions with questions.

Annual legislative appropriations are only one of the many areas in which the Court has been a stepchild for years. As a result, when I came to the Court in January of 1983, much of the Court's equipment was substantially out-of-date. The fanciest typewriter in the building was an IBM Correcting Selectric, a veritable dinosaur. Every day it seemed the Chief would solicit my ideas of things that might be done to improve the Court. It was part of his genuine effort to make me feel important and a part of the Court. For several weeks my response was the same. It would be presumptuous of me to suggest how the Court ought to run its business. Finally I got up my nerve and pointed out that there were these things called word processors that had been in use in most major law offices around the state for at least a decade. He looked puzzled and explained that his typewriter worked just fine. It reminded me of the time about 1950 or 1951 when I told my father about this new thing called television and he responded, "My radio is doing fine." It is not that the Chief was against modern equipment. It was simply beyond his experience. He had become a chancellor in 1947, had come to the Court in 1964. He had never experienced modern office equipment.

In 1985 he received Mississippi State University's Distinguished Jurist of the Year Award. I remember the occasion well. In announcing the award, the presenter referred to his twin achievements of the rule-making power and separation of powers case. Appropriately, these were described as landmarks in Mississippi jurisprudence. His acceptance remarks and conversations afterwards made clear something I had already suspected. He never knew quite how important these matters were. His instincts exceeded his sense of history. Indeed, he never knew quite how important *he* was. No doubt, in many respects, Neville Patterson was a vain and egocentric man, but he didn't understand that *Alexander v. Allain* really was Mississippi's *Marbury v. Madison*, that his writing it made him Mississippi's John Marshall. And in this was a source of his success, for it gave him a certain incorruptibility.

Holmes said a man must be involved in the passions of his time on pain of being judged not to have lived. Neville Patterson was at the center of the legal passions of his time. He generated some and fueled others. He lived, and his state is the better for it.

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1987 MISSISSIPPI SUPREME COURT REVIEW

ADMINISTRATIVE LAW

During 1987, the Mississippi Supreme Court rendered thirty-nine decisions in the area of administrative law. Among the topics covered by these decisions not receiving textual treatment are professional misconduct,[1] statutes,[2] employment,[3] taxes,[4] workers' compensation,[5] decisions of the Mississippi Public Service Commission,[6] and standing.[7]

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[1] *In re* Collins, 524 So. 2d 553, 559-60 (Miss., 1987)(supreme court may forego request of Mississippi Commission on Judicial Performance and impose sanctions it deems appropriate against judge in violation of code of Judicial Conduct); Foote v. Mississippi State Bar Ass'n, 517 So. 2d 561, 566-67 (Miss. 1987)(penalties levied against attorney will not be reversed when not shown to be inconsistent with prior court rulings against similarly situated attorneys); *In re* Hearn, 515 So. 2d 1225, 1228 (Miss. 1987)(Mississippi Commission on Judicial Performance's finding of violation of Code of Judicial Conduct by judge will be accepted if supported by clear and convincing evidence); *In re* Cooksey, 515 So. 2d 957, 959 (Miss. 1987)(supreme court entered order approving commission's recommendations for public reprimand of judge found in violation of Code of Judicial Conduct); Mississippi State Bar Ass'n v. Cotter, 512 So. 2d 1288, 1290-91 (Miss. 1987)(attorney may be disbarred for passing bad checks); Mississippi State Bar Ass'n v. Attorney L., 511 So. 2d 119, 125 (Miss. 1987)(attorney may plead fifth amendment as defense in hearing before Complaint Tribunal if information sought is incriminating); An Attorney v. Mississippi State Bar Ass'n, 508 So. 2d 1120, 1124 (Miss. 1987)(disbarment of attorney not proper where attorney denies allegations and only evidence against him was oral statements and confessions made by him during criminal investigation); Mississippi Bd. of Psychological Examiners v. Hosford, 508 So. 2d 1049, 1053 (Miss. 1987)(post-hearing withdrawal of complaint by complaining party will not negate findings of violation of psychologist-patient privilege by Board).

[2] Board of Trustees of State Inst. of Higher Learning v. Van Slyke, 510 So. 2d 490, 492 (Miss. 1987)(under Mississippi Public Records Act, venue in action against administrative body is proper where body resides); DeSoto County School Bd. v. Garrett, 508 So. 2d 1091, 1093 (Miss. 1987)(School Employment Procedures Act entitles employee terminated from present position, but offered different position at lower pay, to hearing concerning demotion); Board of Trustees of Pascagoula Mun. School Dist. v. Doe, 508 So. 2d 1081, 1085 (Miss. 1987)(Education for All Handicapped Children Act limits school's power to remove handicapped children from school; child subject to Act has right to due process hearings and administrative review of hearings; child also has right to appeal to court, either state or federal, with competent jurisdiction); Waste Control, Inc. v. Tart, 506 So. 2d 286, 289 (Miss. 1987)(county board of supervisors's resolutions concerning maximum load and weight limits complying with MISS. CODE ANN. §§ 65-7-43, -45 (1972) are enforceable); Cox v. Jackson Mun. Separate School Dist., 503 So. 2d 265, 267-268 (Miss. 1987)(notice requirement of Emergency School Leasing Authority Act of 1986 is

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constitutionally adequate and forecloses all complaints occurring to valid, final decree).

[3] Spradlin v. Board of Trustees of Pascagoula Mun. Separate School Dist., 515 So. 2d 893, 898 (Miss. 1987)(decision of school board to terminate employee is neither arbitrary nor capricious when supported by substantial evidence of at least one valid ground for dismissal); Mississippi State Forestry Comm'n v. Piazza, 513 So. 2d 1242, 1249-50 (Miss. 1987)(employee may be transferred when in the best interest of Commission or upon employee's request); Melody Manor, Inc. v. McLeod, 511 So. 2d 281, 283 (Miss. 1987)(circuit court erred in reversing finding of review board based upon substantial evidence that employee voluntarily quit without good cause); Peterson v. City of McComb, 504 So. 2d 208, 211 (Miss. 1987)(intermediate court can only sit as court of review upon all issues before administrative agency and cannot determine questions undecided at trial); Bruner v. University of S. Miss., 501 So. 2d 1113, 1116 (Miss. 1987) (university cannot enter into valid employment contract with individual absent nomination by school's president and approval by Board of Trustees of State Institutions of Higher Learning).

[4] Mississippi State Tax Comm'n v. 3300 Corporation, 515 So. 2d 912, 913-14 (Miss. 1987)(statute of limitations quits running against Tax Commission once Commission files notice of impending tax examination); General Motors Corp. v. Mississippi State Tax Comm'n, 510 So. 2d 498, 502 (Miss. 1987)(prior to amendment, MISS. CODE ANN. § 27-21-9 allowed privileged taxpayer to claim entire privilege tax credit, regardless of whether credit exceeded privileged corporate subsidiary's income tax attributable to Mississippi operations, and credit inured to benefit of affiliated group via consolidated returns); Mississippi State Tax Comm'n v. Dyer Inv. Co., 507 So. 2d 1287, 1291-92 (Miss. 1987)(where taxpayer used installment method of accounting to defer gain, under then-existing franchise tax statutes, deferred gain will not be characterized as undivided profits and will not be added to taxpayer's franchise tax base).

[5] Stevens v. FMC Corp., 515 So. 2d 928, 931 (Miss. 1987)(Mississippi Workers' Compensation Act is exclusive remedy of employee injured while working; suit sounding in negligence may not be maintained); White v. Superior Prod. Inc., 515 So. 2d 924, 927 (Miss. 1987)(supreme court will defer to findings of fact of Commission if substantial evidence exists supporting findings); Sawyer v. Johnson, 510 So. 2d 482, 482-83 (Miss. 1987)(same); Sawyer v. Mason, 510 So. 2d 480, 481 (Miss. 1987)(employer is to be given credit against any award made to injured employee or his dependents for sums received in settlement of third party actions and direct suits against employer); M & J Oil Co. v. Dependents of Wilson, 507 So. 2d 1292, 1293 (Miss. 1987)(maximum attorney fee in workers' compensation case is ⅓ of recovery); General Elec. Co. v. McKinnon, 507 So. 2d 363, 367 (Miss. 1987)(claimant under Mississippi Workers' Compensation Act may collect separate awards for separate and concurrent injuries); Sawyer v. Head, 505 So. 2d 1199, 1200 (Miss. 1987)(dependency is fact to be determined upon death of claimant and one is dependent only if he relies upon employee in whole or in part for support); Davis v. Scotch Plywood Co. of Miss., 505 So. 2d 1192, 1196-97 (Miss. 1987)(conflicting medical testimony should be reconciled so as to find no conflict between examinations done at different times on injured employee).

[6] Dorman v. Rowell, 515 So. 2d 1214, 1216 (Miss. 1987)(security interest may be granted in certificate without approval of Public Service Commission); State v. Mississippi Pub. Serv. Comm'n, 506 So. 2d 978, 984-86 (Miss. 1987)(Public Service Commission must review prudency of any investment by utility company before granting rate increases based upon investment).

[7] *See* Mississippi High School Activities Assoc., Inc. v. Farris, 501 So. 2d 393, 398

Cases receiving textual treatment include decisions concerning the liability of an employer who has received benefits from another source,[8] the liability of a contractor who agrees to provide workers' compensation insurance for a subcontractor's employees when the subcontractor works on the job as an essential employee and is subsequently injured,[9] the right of an injured, deceased employee's heirs-at-law to receive workers' compensation benefits from his former employer,[10] the preexistence of an injury as a mitigation factor in the determination of workers' compensation benefits,[11] the ability of an election commissioner to run for public office while holding his position as election commissioner,[12] the conflict of interest that arises when a public official contracts with the public body of which he is a member,[13] the ability of a state agency to file suit when the attorney general declines to do so,[14] and the appropriateness of a hearing by the Mississippi Public Service Commission when a permanent and substantial rate increase by a public utility is requested.[15]

I. Workers' Compensation

The Mississippi Supreme Court handed down several decisions concerning benefits recoverable by an injured employee and his dependents during 1987. First, in *Reichhold Chemical, Inc. v. Sprankle*,[16] the Mississippi Supreme Court addressed the issue of whether a preexisting injury should be taken into consideration in determining bene-

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(Miss. 1987)(members of high school athletic team did not have standing to assert school's right of appeal before Mississippi High School Activities Association with regard to school's athletic probation).

[8] Sawyer v. Head, 510 So. 2d 472 (Miss. 1987); *see infra* notes 19-23 and accompanying text.

[9] Champion Cable Constr. Co. v. Monts, 511 So. 2d 924 (Miss. 1987); *see infra* notes 29-33 and accompanying text.

[10] Dependents of Nosser v. Natchez Jitney Jungle, 511 So. 2d 141 (Miss. 1987); *see infra* notes 24-28 and accompanying text.

[11] Reichhold Chem., Inc. v. Sprankle, 503 So. 2d 799 (Miss. 1987); *see infra* notes 16-18 and accompanying text.

[12] Meeks v. Tallahatchie County, 513 So. 2d 563 (Miss. 1987); *see infra* notes 44-54 and accompanying text.

[13] State ex rel. Pittman v. Ladner, 512 So. 2d 1271 (Miss. 1987); *see infra* notes 55-67 and accompanying text.

[14] Frazier v. State ex rel. Pittman, 504 So. 2d 675 (Miss. 1987); *see infra* notes 34-43 and accompanying text.

[15] State v. Mississippi Public Serv. Comm'n, Nos. 57,104, 57,123, slip op. (Miss. December 2, 1987); *see infra* notes 68-75 and accompanying text.

[16] 503 So. 2d 799 (Miss. 1987).

fits awardable to an employee injured while on the job.[17] In determining that such a pre-existing injury should be considered in establishing an employee's benefits, the court concluded that the Workers' Compensation Commission must apportion the injury between the pre-existing condition and the work-related injury.[18]

The Mississippi Supreme Court further limited an injured employee's recovery for a work-related injury in *Sawyer v. Head*.[19] In *Sawyer*, the court upheld the findings of an administrative law judge and held that the Workers' Compensation Commission erred in restricting the credit to the employer and its carrier only to settlements reached by the dependents with a third party.[20] The Commission refused to grant a credit to the employer for a settlement reached between it and the deceased employee's dependents.[21] Having reviewed the purpose of the Workers' Compensation Act, the court concluded that it was contrary to the purpose of the Act for an injured employee or his dependents to be awarded compensation both through the act and through the pursuit of a separate, unrelated lawsuit.[22] Accordingly, the court adopted the administrative law judge's ruling that the employer and carrier of worker's compensation insurance should be given credit against the previous award to an injured employee or his dependents for money received by them in settlement of third party actions and direct suits against the employer arising out of the accident which caused the injury.[23]

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[17] *Id.* at 803. Raymond L. Sprankle, Sr. filed for workers' compensation benefits alleging that because he was engulfed by a cloud of ammonia gas while at work, he was 100% permanently and totally disabled. *Id.* at 800.

[18] *Id.* at 803. At his hearing before an administrative law judge, it was found that Sprankle had suffered from minor exposure to ammonia gas, but that his disability resulted from an already diagnosed case of emphysema. Sprankle appealed to the Workers' Compensation Commission which reversed the findings of the administrative law judge and awarded Sprankle $98 per week and all medical expenses associated with the ammonia exposure. An appeal by Reichhold Chemical to the Circuit Court of Harrison County resulted in an affirmance when the circuit judge ruled that he could not, as a matter of law, find that the awarding of compensation was not based on substantial evidence. *Id.* at 800. In its opinion, the Mississippi Supreme Court held that the appellate court should yield to the findings of the Commission with regard to compensation. However, the court at the same time found that the Commission had erred in finding that the benefactor was permanently disabled and remanded the case for further inquiry into the apportionment of his injury between his work-related injury and his pre-existing condition. *Id.* at 802-03.

[19] 510 So. 2d 472 (Miss. 1987). Rufus Head was involved in an automobile accident while working for Lakeland Plantations. At the time of the accident, he was enroute to lunch in a company-owned vehicle. Head was killed in the accident. In 1975, suit was filed by the dependents of Head against Head's employer, the estate of the driver of the vehicle in which Head was riding, the farm's manager, and the owners of the second vehicle involved in the wreck. An out-of-court settlement agreement was reached for $11,000. *Id.* at 473-74.

[20] *Id.* at 480. An administrative law judge presiding over Workers' Compensation Commission hearings held that at the time of the accident, Rufus Head was acting within the scope of his employment and that he left surviving him as dependents his mother, three sisters and two brothers. However, the administrative law judge also held that the employer and carrier of workers' compensation insurance should be given credit against the previous award to the dependent of Rufus Head for money received by them in settlement of third party actions and direct suits against the employer arising out of the accident. *Id.* at 474.

[21] *Id.* Upon appeal to the full Workers' Compensation Commission, the Commission

Besides limiting benefits awardable in workers' compensation cases, the Mississippi Supreme Court also limited the possible benefactors of such an award in *Dependents of Nosser v. Natchez Jitney Jungle.*[24] The court interpreted section 71-3-25[25] of the Mississippi Code to exclude an injured, deceased employee's non-dependent heirs-at-law from receiving benefits otherwise payable to the dependents of the de-

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held that the employer and its carrier should only be allowed a credit against their workers's compensation coverage to the extent of the amount paid the dependents pursuant to their settlement agreement against the owner of the second vehicle involved in the wreck. The findings of the Commission were affirmed by the Circuit Court of Holmes County. *Id.*

[22] *Id.* at 479-80.

[23] *Id.* at 480. The court upheld the findings of the administrative law judge in toto. *See also* Sawyer v. Mason, 510 So. 2d 480, 481 (Miss. 1987)(employer is to be given credit against any award made to injured employee or his dependents for sums received in settlement of third party actions and direct suits against employer).

[24] 511 So. 2d 141 (Miss. 1987). The decedent was killed during a robbery of a grocery store of which he was an assistant manager. He left no dependents, but his parents and siblings sought to recover under the Mississippi Workers' Compensation Act as the decedent's heirs-at-law. Recovery of benefits was denied, and an appeal followed. *Id.* at 142.

[25] MISS. CODE ANN. § 71-3-25 provides, in pertinent part:

> If the injury caused death, the compensation shall be known as a death benefit and shall be payable in the amount and to or for the benefit of the persons following:
>
> (e) If there be no surviving spouse or child, . . ., then for the support of grandchildren or brothers and sisters, if dependent upon deceased at the time of the injury, . . ., and for the support of each parent or grandparent of the deceased, if dependent upon him at the time of injury. . .
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> ****
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> (g) All questions of dependency shall be determined as of the time of the injury. A surviving spouse, child or children shall be presumed to be wholly dependent. All other dependents shall be considered on the basis of total or partial dependence as the facts may warrant.

MISS. CODE ANN. § 71-3-25 (Supp. 1987).

ceased employee.[26] According to the court, the purpose of the Workers' Compensation Act is to provide a recovery to persons directly and financially dependent upon the decedent.[27] Therefore, the court concluded that since none of the decedent's heirs-at-law relied upon him for support, the recovery of benefits by them was properly denied by the Commission.[28]

Finally, in *Champion Cable Construction Co. v. Monts*,[29] the court addressed the issue of a contractor's responsibility to a subcontractor for an injury occurring to the sub-contractor while working at the construction site.[30] The court held that where a contractor agrees to provide workers' compensation insurance to a subcontractor, and the subcontractor works on the job as an essential employee, that subcontractor is entitled to receive workers' compensation benefits from the contractor and his carrier if he is subsequently injured while in the course of his employment.[31] In so ruling, however, the court based its decision upon the premise that the subcontractor had no knowledge that he was specifically not included in the workers' compensation coverage.[32] Therefore, the court apparently would have reached an opposite conclusion if the subcontractor had known that he was not included in the coverage.[33]

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[26] *Nosser*, 511 So. 2d at 144. In so ruling, the court relied upon decisions of various other state courts in interpreting their workers' compensations acts. *See* Slagle v. Reynolds Metals Co., 344 So. 2d 1216, 1217-18 (Ala. 1977)(employer immune from claims of non-dependents); Atchison v. May, 10 So. 2d 785, 787-88 (La. 1942)(act limits recovery to dependents who have or will suffer economic loss as result of death of decedent). *But see* Park v. Rockwell Int'l Corp., 436 A.2d 1136, 1140 (N.H. 1981)(value of life of deceased employee without dependents is no less than that of deceased employee with dependents.)

[27] *Nosser*, 511 So. 2d at 144.

[28] *Id.*

[29] 511 So. 2d 924 (Miss. 1987).

[30] *Id.* at 926-28. Champion Cable Construction contracted with Byers Communication to run and rig a cable system in Florida. When Champion fell behind in its work, it contracted with Turner Monts. Monts provided two crews to Champion, of which he was a working member. Monts provided his crews' equipment and Champion agreed to cover all of Monts' men with general liability insurance and workers' compensation coverage. Subsequently, while rigging the wire, Monts fell from a pole. Monts sought recovery from Champion's workers' compensation insurer. *Id.* at 925.

An administrative law judge found that Monts was an employee of Champion and awarded him benefits. The Workers' Compensation Commission found, however, that Monts was a subcontractor and reversed the judge's order. On appeal to the Circuit Court of Pontotoc County, the Commission's decision was reversed and Monts was again found to be an employee entitled to benefits. *Id.*

[31] *Id.* at 928-29. In following the substantial evidence test, the court ruled that the circuit court erred in overturning the Commission's finding of fact that Monts was a subcontractor and not an employee. However, although the court found Monts to be a subcontractor, it allowed him to recover from Champions' insurer. According to the court, under the facts of the case, Monts was acting as a working member of one of the two crews contracted by Champion. Therefore, as such a member, he was entitled to coverage under the agreed upon workers' compensation plan. *Id.*

II. PROFESSIONAL RESPONSIBILITY

In 1987, three significant decisions of the Mississippi Supreme Court dealt with the areas of professional responsibility and ethics. *Frazier v. State ex rel. Pittman* was probably the most important of the three.[34] In *Frazier*, various local and state officials were alleged to be in violation of Article 4, section 109 of the Mississippi Constitution of 1890 which prohibits public officials from being contractually interested, either directly or indirectly, with the political subdivision of which they are a part.[35] After the Attorney General declined to bring suit against some of these individuals, the Mississippi Ethics Commission initiated an action against the remainder in the Chancery Court of the First Judicial District of Hinds County.[36] A final decree, which held

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[32] *Id.* at 928; *see also* American Sur. Co. v. Cooper, 222 Miss. 429, 76 So. 2d 254, 256 (1954)(subcontractor is entitled to receive workers' compensation benefits from contractor if subsequently injured, provided he has no knowledge that he is not specifically included in coverage).

[33] 511 So. 2d at 928.

[34] 504 So. 2d 675 (Miss. 1987).

[35] *Id.* at 678. MISS. CONST. art. IV, § 109 provides:

> No public officer or member of the legislature shall be interested, directly or indirectly, in any contract with the state, or any district, county, city, or town thereof, authorized by any law passed or order made by any board of which he may be or may have been a member, during the term for which he shall have been chosen, or within one year after the expiration of such term.

MISS. CONST. art. IV, § 109.

[36] *Frazier*, 504 So.2d at 678. Two suits were brought in the Chancery Court of the First Judicial District of Hinds County. In the first suit, the state brought suit against Hillman T. Frazier and Bill F. Knox for allegedly violating MISS. CONST. art. iv, § 109. In the second suit, brought by the Mississippi Ethics Commission, it was alleged that Donald N. Logan, James D. Nunnally, Manuel Kellebrew, Douglas L. Anderson and Perrin H. Purvis likewise were in violation of the same section of the Constitution. Both the State and the Commission sought declaratory relief. The Commission also sought restitution from the defendants named in their suit for all compensation received from the state in violation of § 109. *Id.*

Hillman T. Frazier is a state representative for the 67th District of the Mississippi Legislature. While serving in this position, Frazier was also employed by Jackson State University. During the years 1984 and 1985, Representative Frazier voted in favor of two bills making fiscal appropriations to the Board of Trustees of State Institutions of Higher Learning for disbursement by the Board to Jackson State and other state institutions. Frazier's compensation for his contract with Jackson State came from these approvarious statutes purportedly authorizing such conduct unconstitutional,[37] was entered by the chancellor against all the officials and an

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priations. *Id.*

Bill F. Knox was elected as a Supervisor, District 2 of the Board of Supervisors of Panola County. While serving on the Board, Knox was also acting as an officer and stockholder of various banks in Panola County serving as county depositories. *Id.* at 679.

Donald N. Logan, principal of Harper McGaughan Elementary School, was elected to an alderman-at-large position for the City of Long Beach in 1982. From 1982 until 1985, Logan voted on four *ad valorem* tax levies which were partially used to pay the local portion of the teacher's salaries. Of these four levies, three were mandatory upon the order of the board of trustees of the school district and one was discretionary. *Id.* at 679-80.

James D. Nunnally, a state representative for the 4th District since 1971, was also employed as a teacher in the Benton County School District while serving as a representative. Nunnally's wife was employed as a public school teacher by South Tippah County Consolidated School District. From March 1984 to March 1985, Nunnally voted in favor of two appropriations to the State Department of Education for disbursement by the department to the two school districts for fiscal years 1985 and 1986. Nunnally, however, abstained from voting on a bill revising the teacher's salary schedule and an increase in the minimum education program allotment. *Id.* at 680-81.

Manuel Killebrew, while serving as a supervisor on the Board of Supervisors of Quitman County, was employed as a teacher at Quitman County High School. During his term on the county board, Killebrew voted in favor of two mandatory *ad valorem* tax levies and two discretionary levies. These taxes were used to support the Quitman County School District. *Id.* at 681-82.

Douglas Anderson, a state senator for the 27th District of the Mississippi Legislature, voted in favor of two appropriation bills to the Board of Trustees of State Institutions of Higher Learning for disbursement to Jackson State University and other institutions of higher learning for the fiscal years 1985 and 1986. At the time, Anderson was also an Assistant Professor of Mathematics at Jackson State University. *Id* at 682.

Perrin H. Purvis, president and shareholder of P.I.A., Inc., a Mississippi corporation in the business of selling insurance, had been a state senator for the 6th District of the Mississippi Legislature since 1963. In 1984 and 1985, Purvis voted in favor of two bills authorizing appropriations to the Tombigbee River Valley Water Management District for the support and maintenance of the district for fiscal years 1985 and 1986. In 1985, P.I.A. entered into a bid for the supplying of insurance coverage for the district and its bid was accepted by the District. Payment for this contract was to come from money appropriated by the Mississippi Legislature. Upon notice of the suit by the Ethics Commission against Purvis, the policy was cancelled. *Id.*

[37] *Id.* at 687-89. According to the State and the Ethics Commission, the activities of each of the defendants violated § 109. However, MISS. CODE ANN. § 25-4-105(3)(h) provides statutory authority for the conduct of Frazier, Logan, Nunnally, Killebrew and Anderson. MISS. CODE ANN. § 25-4-105(3)(a) provides statutory authority for Knox to be an officer and shareholder in the Panola County banks while serving as a member of the County Board of Supervisors. The conduct of Purvis, while acting as a state senator, was protected by MISS. CODE ANN. § 25-4-105(3)(b). The State and the Commission claimed that insofar as these subsections of § 25-4-105 authorized the conduct of these elected officials, the statute violated § 109 and was therefore unconstitutional. Conversely, the

appeal followed.[38] In its majority opinion, the Mississippi Supreme Court held that the chancellor correctly ruled with regard to the authority of the Commission to bring suit against the elected officials.[39] In so doing, the court ruled that although the proper party to bring suit against such officials is the State through the Attorney General, if the Attorney General declines to bring a suit referred to it by the Commission, and the matter is of a serious concern to the state government, then the Commission itself could bring suit if it determined that its duties and responsibilities so required.[40] After so ruling, the court then turned to each individual's case and addressed it separately.[41] Separate

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defendants in the suit filed by the Commission claimed that the Commission did not have the authority to file suit and moved for dismissal. *Frazier*, 504 So. 2d at 686.

[38] *Frazier*, 504 So. 2d at 689. In denying the motion for dismissal and upon the entering of a final decree, the Chancery Court of the First Judicial District of Hinds County found all the defendants to be in violation of § 109 and held that any statutory authority purporting to authorize their conduct was unconstitutional. In so holding, however, the court refused the Ethics Commission's plea for restitution and declined to enjoin the defendants from divesting themselves of any contractual interest or resigning from their public office. All defendants except Purvis appealed. The Commission cross-appealed the court's denial of restitution. *Id.*

[39] *Id.* at 704-05.

[40] *Id.* at 691-93. According to the court, it should be the judiciary, not the attorney general, which should determine whether the agency is representing the people of the state by bringing such a suit. *Id.*

[41] *Id.* The court held that the conduct of Anderson, Frazier and Nunnally, while serving in the legislature, violated § 109 of the Mississippi Constitution. Furthermore, the court held that insofar as § 25-4-105(3)(h) authorized their dual employment, that section was at odds with the constitution and therefore void. The declaratory judgment as to them was affirmed; however, as to the employment of Nunnally's wife as a public school teacher receiving a salary from appropriations made by the Mississippi legislature, the activities of Nunnally while serving as a legislator did not violate § 109. Accordingly to the court, it was never envisioned that § 109 would be carried to such an extreme as to prevent a public school teacher's spouse from serving in state government. *Id.* at 704-05.

The court also held that the contracts of Logan and Killebrew with the public schools systems violated § 109 insofar as their salaries were derived from discretionary local tax levies. Any exception to this holding carved out by § 25-4-105(3)(h) was unconstitutional. However, the court further held that Logan was not in violation of § 109 in voting on tax levies that were mandatory in nature. According to the court, it was never the intent of the authors of § 109 to penalize non-discretionary activity by public officials. Therefore, the chancery court erred in finding Logan in violation of § 109 with regard to these mandatory tax levies. *Id.*

As to Knox, the court held that a county board member, acting as a stockholder, director, and officer of a county bank, violates § 109 by authorizing any contract which makes that bank a county depository. The court determined that Knox's authority to negotiate depository contracts with banks was discretionary and that he therefore violated § 109. Furthermore, the exception provided by § 25-4-105(3)(a) was unconstitutional. *Id.*

opinions were authored by Justices Sullivan[42] and Robertson.[43]

In *Meeks v. Tallahatchie County*,[44] the court was asked to review the actions of a county election commissioner running for office while holding his commission position.[45] While serving on the Election Commission of Tallahatchie County, a commissioner filed for qualification as a candidate for the Democratic Party nomination for the office of Justice Court Judge.[46] The Tallahatchie County Democratic Party Executive Committee denied his petition for qualification.[47] Suit was filed by the Commissioner in the Circuit Court of Tallahatchie County, but

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Finally, the court affirmed the chancellor's denial of restitution to the Ethics Commission. The court held that a public official, acting in good faith reliance upon a statute later ruled unconstitutional could not be held civilly liable for conduct authorized by the statute. Finding no bad faith in the present situation, the court affirmed the chancellor's findings as to denial of restitution. *Id.* at 704; *see also* Golden v. Thompson, 194 Miss. 241, 11 So. 2d 906, 907 (1942)(public official may not be held civilly liable when acting in good faith and in reliance upon statute later ruled unconstitutional).

[42] *Frazier*, 504 So. 2d at 719. Justice Sullivan authored a separate opinion concurring in part and dissenting in part. In his opinion, Justice Sullivan addressed the meaning of "indirect" within § 109. Contrary to the majority opinion, Justice Sullivan concluded that defendant Nunnally clearly was subjected to § 109 via the employment of Mrs. Nunnally, a public school teacher. This conclusion was reached on the premise that such employment as a school teacher clearly created an "indirect interest" in the appropriations bill from Nunnally's standpoint. Justice Sullivan further concluded that the majority opinion erred in distinguishing between "discretionary" and "mandatory" acts. Justice Sullivan's proposition was based on the premise that "voting" had nothing to do with § 109 and hence mere membership in a public entity was sufficient to subject one to an application of § 109. *Id.* at 720-21.

[43] *Id.* at 706. In a separate opinion in which he concurred in part and dissented in part, Justice Robertson advocated judicial deference to the legislative enactments. *Id.* at 708-09. Justice Robertson assumed arguendo that the "interest" test of § 109 was met and then addressed what he believed to be the problem with the majority opinion. The analysis by Justice Robertson focused on the word "authorized" as contained in § 109. Justice Robertson concluded that funding by way of an appropriation bill passed by a given entity was not tantamount to "authorized" as addressed by § 109. For example, Justice Robertson argued that the Board of Trustees of State Institutions of Higher Learning "authorized" the contracts with defendants Anderson and Frazier and that the legislature merely funded contracts authorized by the Board. Hence a strict interpretation of "authorized" would not encompass "funding" and therefore § 109 would not apply so as to override the statutes. *Id.* at 711-14.

[44] 513 So. 2d 563 (Miss. 1987).

[45] *Id.* at 563-64. Eddie Meeks was elected to the Elections Commission of Tallahatchie County in 1984. *Id.*

[46] *Id.* Meeks tendered his elections commission resignation two weeks after filing his petition for qualification as a candidate for the office of justice court judge. *Id.*

[47] *Id.* at 564. At a hearing before the Tallahatchie County Democratic Party Executive Committee, his certification was denied. Hearing of his denial, Meeks appeared before the commission and stated his position. Again, certification was denied. *Id.*

the court refused to grant any relief.[48] An expedited appeal to the Mississippi Supreme Court followed.[49] Following a discussion of whether the commissioner was accorded his right to due process by the Tallahatchie County Democratic Party Executive Committee,[50] the court affirmed the decision of the circuit court.[51] According to the court, section 23-15-217 of the Mississippi Code[52] is not vague in its wording and clearly sets forth the instances in which an election commissioner may not run for office.[53] By so ruling, the court concluded that any person serving as an election commissioner is barred from seeking another elected position so long as his position on the commission remains unexpired.[54]

Finally, in *State ex rel. Pittman v. Ladner*,[55] the court once again addressed the issue of conflict of interest between a public official's duty as a servant of the people and his private interests.[56] In violation of section 37-11-27 of the Mississippi Code,[57] the Harrison County

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[48] *Id.* In his petition, Meeks requested that the court compel the committee to include his name on the ballot. *Id.*

[49] *Id.*

[50] *Id.* at 565-66. According to the court, although unorthodox in its procedure, the Executive Committee meeting in which Meeks' certificate was denied did not violate his rights to due process of law. Furthermore, according to the court, Meeks' appearance before the Commission and the presentation of his case was outcome determinative with regard to the issue of due process. *Id.*

[51] *Id.* at 569.

[52] MISS. CODE ANN. § 23-15-217 (Supp. 1987) provides:

> A commissioner of election of any county shall not be a candidate for any office at any election for which he may have been elected or with reference to which he has acted as such; and all votes cast for any such person at such election shall be illegal and shall not be counted, except that he may be a candidate for the office of county election commissioner.

Id.

[53] *Meeks*, 513 So. 2d at 566-67. The court concluded that the statute clearly set forth the instances in which an election commissioner may not run for office. Under the court's interpretation of the statute, Meeks clearly fell within the statute's position, regardless of whether he resigned from his election commission position. *Id.* at 568.

[54] *Id.* at 569.

[55] 512 So. 2d 1271 (Miss. 1987).

[56] *Id.* at 1272.

[57] *Id.* MISS. CODE ANN. § 37-11-27 (1972) provides:

> It shall be unlawful for any member of the board of trustees of any school district, any member of the county board of education, the county superintendent of education or any superintendent, principal, teacher, or employee of a county board of education or any school district to have or own any direct or indirect interest individually or as agent or employee of any person, partnership, firm, or corporation in any contract made or let by the county board of education, the county superintendent of education or the board of trustees of

School Board awarded a contract to a bidder which employed a member of the board.[58] In other instances, the Board was found to have entered into contracts with other bidders without obtaining the then statutorily required three bids per contract.[59] The State of Mississippi, acting by and through the Attorney General and State Auditor, filed a complaint in the Chancery Court of Hancock County alleging violation of these statutes by the school board and superintendent of public

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> the school district for the construction, repair, or improvement of any school facility, the furnishing of any supplies, materials, or other articles, the doing of any public work or the transportation of children or upon any sub-contract arising therefrom or connected therewith in any manner. Any contract entered into in violation of the provisions of this section shall be void and of no effect. Any person who shall authorize or enter into any contract in violation of the provisions hereof, or who shall knowingly or willfully pay out or receive any money upon any such contract shall be civilly liable for the amount so paid or received, and, in the case of an official who has furnished a bond, the surety upon such bond shall likewise be liable for such amount. In addition thereto, any person who shall violate the provisions of this section shall be guilty of a misdemeanor and, upon conviction, shall be punished by a fine of not less than one hundred dollars ($100.00) nor more than five hundred dollars ($500.00), or by imprisonment in the county jail not less than thirty days nor more than ninety days, or by both such fine and imprisonment, in the discretion of the court. Nothing herein shall be construed to prohibit any employee of a county board of education or any school district, other than a superintendent or principal, from being employed to drive a publicly owned school bus.

Id.

[58] *Ladner*, 512 So. 2d at 1273. The contract was made following a tornado in Harrison County which damaged Gulfview Elementary School. The contract was only entered into after consulting with the board's attorney. The attorney advised the board that such a contract would not be violative of the section so long as the board member/employee did not take part in the vote. *Id.*

[59] *Id.* These contracts, just as the one entered into with Ladner's employer, were made following the tornado which damaged Gulfview Elementary School. MISS. CODE ANN. § 31-7-42 (1972) required:

> In cases of emergency, by order spread upon the minutes of the board or other governing authority stating the nature of such emergency in which an itemized statement of work required to be done or required equipment, heavy equipment, or supplies has been submitted to at least three (3) reputable concerns licensed to do business in the State of Mississippi for the work, equipment, or supplies sought, such a an emergency or urgent contract or purchase may be made from the lowest and best bidder. . .

MISS. CODE ANN. § 31-7-42 (1972).

MISS. CODE ANN. § 31-7-42 was subsequently repealed, effective January 1, 1981. A different emergency procedure was provided in MISS. CODE ANN. § 31-7-13(e) which did not required competitive bids in emergency situations. This section was further modified and recodified as MISS. CODE ANN. § 19-13-37(2). *Ladner*, 512 So. 2d at 1274.

schools.[60] A partial summary judgement was entered against the State with regard to the violation of the three bid rule and for the State on the issue of the board member's conflict of interest.[61] Damages and penalties totaling $53,784.32 were levied against the school board members and superintendent.[62] An appeal by all parties followed.[63] In its opinion, the Mississippi Supreme Court affirmed the granting of partial summary judgments to both the State and the public officials.[64] According to the court, by contracting with a company employing a member of the Board, the Board acted in clear violation of section 37-11-27.[65] Furthermore, the court concluded that the chancellor was correct in ruling that the State had acquired no vested right prior to the repeal of section 31-7-43 and therefore could not assert it at this time.[66] Therefore, absent a contract or property right, the State had no enforceable interest without entry of a final judgment before the repeal of the statute.[67] Although the court held that the chancellor ruled correctly on these two issues of law, it reversed and remanded the case to the chancery court for the establishment of a record upon which a determination could be made whether the penalties levied against the officials were proper.[68]

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[60] *Ladner*, 512 So. 2d at 1273. In its suit, the State sought to recover repayment of all money spent by the board with regard to these contracts and a penalty from each Board member as provided by MISS. CODE ANN. § 19-13-37(2). *Ladner*, 512 So. 2d at 1274.

[61] *Id.* According to the lower court, the three competitive bid rule was repealed prior to the State acquiring any vested rights in it. *Id.*

[62] *Id.* On the conflict of interests claim, judgment was entered against the defendants in the sum of $27,784.32. The court further assessed a penalty of $5,000 each against four Board members and the superintendent and $4,000 against a Board member who was absent from the meeting in which the contract was granted to Ladner's employer. *Id.*

[63] *Id.*

[64] *Id.* at 1281.

[65] *Id.* at 1280. The fact that the Board members consulted with their attorney before entering into the contract with Ladner's employer was not outcome determinative. According to the court, the actions of the Board were in clear violation of § 31-11-27 and a partial summary judgment granted to the State on this claim was justifiable. *Id.*

[66] *Id.* at 1277. In so holding, the court followed its earlier established rule that the effect of repealing a statute is to abrogate it as if it never existed. *Id*; *see also* Stone v. Independent Linen Serv. Co., 212 Miss. 580, 586-87, 55 So. 2d 165, 168 (1951)(effect of repealing statute is to abrogate it as completely as if it had never been passed unless repealing statute contains saving clause).

[67] *Ladner*, 512 So. 2d at 1277.

[68] *Id.* at 1281. The court, in its opinion, had no doubt that the uncontradicted facts established the justifiability of a penalty against all six defendants. However, the opinion of the chancellor did not set forth the method by which he arrived at the amounts assessed against each defendant. Therefore, the court vacated the penalties awarded by

III. MISSISSIPPI PUBLIC SERVICE COMMISSION

One case receiving review by the Mississippi Supreme Court after a denial of hearing by the Mississippi Public Service Commission was *State v. Mississippi Public Service Commission.*[69] In *MPSC*, The Mississippi Power Company filed a rate increase request with the Commission for losses incurred by the company during Hurricane "Elena".[70] The Attorney General and two legal aid services filed an objection to the rate increase and requested a hearing over the proposed rate changes.[71] The Commission denied the requested hearing on the basis that "no major revenue changes were involved" in the filing of "a routine change in rates" and approved a "temporary" rate increase of $9,994,135.00.[72] Following a denial of rehearing by the Commission, all aggrieved parties perfected an appeal.[73] Sitting *en banc*, the court concluded that the Commission improperly denied the aggrieved parties a hearing before instituting the rate increases.[74] Finding that a great deal of the rate increases requested by the company were actually permanent in nature, rather than temporary, the court concluded that the

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summary judgment and remanded the case to the chancellor for a full evidentiary hearing upon the penalties. *Id.*

[69] 520 So. 2d 1355 (Miss. 1987).

[70] *Id.* at 1356. Following the interruption of service to 23 counties in southeast Mississippi when Hurricane "Elena" hit the Gulf Coast, the Mississippi Power Company filed a "notice of change in rates" for $16,063,986.00 with the Mississippi Public Service Commission. The rate increase was requested to compensate for losses incurred by the company during the hurricane. Specifically, the increased rates covered expenses for storm damage, an increase in the company's storm reserve fund, and for revenue lost by the company during the power cutoff. *Id.* at 1357.

[71] *Id.* at 1356. The Attorney General, Mississippi Legal Services Coalition, and Southeast Mississippi Legal Services filed an objection to the rate increase, requested a hearing over the proposed increase, and moved for a dismissal of any rate increase. *Id.*

[72] *Id.* at 1357. The Commission approved a temporary rate increase of $9,994,135.00 for a period not to exceed 19 months. The Commission also approved a $536,135.00 annual increase to the company's storm damage reserve account with an amended total permissible accrual of $10,928,400.00. *Id.*

[73] *Id.*

[74] *Id.* at 1358-60. During oral argument, the Commission and the company argued that no evidentiary hearing was required by statute or was needed. In asserting this argument, the Commission relied upon MISS. CODE ANN. § 77-3-47 (1972) as authority for no requirement of a hearing. The court recognized that it had never before addressed this question. However, the court further recognized that whenever a rate increase was contested prior to the one presently requested by the company, the Commission had always granted a hearing to the contestants. Therefore, the court considered the Commission's argument to be somewhat dubious and concluded that the State should have the opportunity to confront the company with regard to the propriety of the requested rate changes. *Public Service Commission*, 520 So. 2d at 1360.

Attorney General was entitled to confront the company with regard to the propriety of the requested rate increases.[75] After so ruling, the court then addressed the various bases of proposed rate increase and their propriety and reversed and remanded the case for a hearing on this issue.[76]

Jack Melvin, Jr.

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[75] *Id.* The court concluded, in its opinion, that many of the rate increases requested by the company were actually permanent in nature, subject only to a cap. *Id.*

[76] *Id.* at 1360-63. The court concluded that a rate increase for storm damages was a proper exception to the general rule that ". . . losses incurred by a utility because an existing rate is inadequate may not be recovered by excessive rates in the future." *Id.* Further, the court concluded that storm reserve funds were a proper charge. However, the court was unwilling to allow recovery by the utility for revenue lost as a result of it having to cease services to its customers during the storm. According to the court, this would amount to a penalty to its customers who were forced to find alternative sources of energy during the shut-off. *Id.*

CIVIL PROCEDURE

The Mississippi Supreme Court handed down fifty-seven cases concerning civil procedure in 1987, of which four will be discussed textually in this comment. Cases not treated textually clarified the recently promulgated Mississippi Rules of Civil Procedure and pre-existing procedure statutes in a number of areas, including admissibility of blood tests results,[1] appeal bonds,[2] appellate review,[3] civil contempt,[4] collateral estoppel and res judicata,[5] continuances,[6] default,[7] directed verdicts,[8] discovery,[9] dismissal of claims,[10] findings by the trial court,[11] full faith and credit,[12] injunctions,[13] intervention,[14] joinder of parties,[15] judgments,[16] jurisdiction,[17] jury view,[18] reformation of jury

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[1] Clark v. City of Pascagoula, 507 So. 2d 70, 75 (Miss. 1987)(despite statutory prohibition against admitting results of blood tests into evidence, no error occurs where test introduced in defense of person tested by his personal representative since prohibition is intended to protect interests of person tested).

[2] Johnson v. Evans, 517 So. 2d 570, 570-71 (Miss. 1987)(party appealing from county court to circuit court must post bond within ten days of entry of final judgment of county court).

[3] Beck Enters. v. Hester, 512 So. 2d 672, 678-79 (Miss. 1987)(on petition for rehearing, supreme court will not consider issues not raised on appeal).

[4] Jones v. Hargrove, 516 So. 2d 1354, 1357-58 (Miss. 1987)(contemnor may not be jailed where failure to pay child support results from inability to pay).

[5] *In re* K.M.G., 500 So. 2d 994, 997 (Miss. 1987)(where child abuse claim was fully litigated in foreign court, principle of collateral estoppel applies to bar relitigation in Mississippi; full faith and credit must be given to foreign judgment).

[6] Terrell v. Rankin, 511 So. 2d 126, 129 (Miss. 1987)(untimely filed Miss. R. Civ. P. 56(f) motion for continuance supported by affidavit sufficiently explaining delay should be granted where opposing party fails to object at time of filing and documents causing delay are untimely produced); Hudson v. Parvin, 511 So. 2d 499, 500 (Miss. 1987)(Miss. R. Civ. P. 56(f) continuance should be granted where movant's newly acquired counsel has insufficient time to prepare response to nonmovant's motion for summary judgment).

[7] H & W Transfer and Cartage Serv., Inc. v. Griffin, 511 So. 2d 895, 898-99 (Miss. 1987)(denial of Miss. R. Civ. P. 60(b) motion to set aside default judgment within discretion of trial judge); Pointer v. Huffman, 509 So. 2d 870, 873-74 (Miss. 1987)(default judgment may be entered on issue of liability alone); Vining v. Mississippi State Bar Ass'n, 508 So. 2d 1047, 1048 (Miss. 1987)(default judgment proper in attorney disciplinary proceeding where requirements of Miss. R. Civ. P. 55 are satisfied).

[8] Collins v. Ringwald, 502 So. 2d 677, 678-79 (Miss. 1987)(where evidence is conflicting in suit arising from automobile collision, directed verdict is improper because question of liability should be submitted to jury).

[9] Williams v. Puryear, 515 So. 2d 1231, 1233-34 (Miss. 1987)(trial court may dismiss claim with prejudice pursuant to Miss. R. Civ. P. 37(b)(2)(C) where plaintiff willfully refuses to comply with discovery); Williams v. Dixie Elec. Power Ass'n, 514 So. 2d 332, 335-37 (Miss. 1987)(wrongfully withheld discoverable materials may not be admitted into evidence at trial); Harris v. General Host Corp. 503 So. 2d 795, 798 (Miss. 1987)(Miss. R.

Civ. P. 26(b)(4)(A)(i) imposes duty upon litigant to provide complete responses to interrogatories regarding expert witnesses and to timely supplement those responses should it become necessary to do so); Kern v. Gulf Coast Nursing Home, Inc., 502 So. 2d 1198, 1200 (Miss. 1987)(discovery may not be used to compel disclosure of trial witnesses, only occurrence witnesses).

[10] Ainsworth v. Callon Petroleum Co., 521 So. 2d 1272, 1274 (Miss. 1987)(ruling on Miss. R. Civ. P. 41(b) motion practically equivalent to finding of fact; supreme court will apply substantial evidence/manifest error test on review); Shepherd v. Delta Medical Center, 502 So. 2d 1188, 1192 (Miss. 1987)(Miss. R. Civ. P. 41(a)(2) requires trial court to voluntarily dismiss action upon plaintiff's motion where erroneous exclusion of evidence necessitated plaintiff's request for dismissal).

[11] Tricon Metals and Servs., Inc. v. Topp, 516 So. 2d 236, 239 (Miss. 1987)(trial court "generally should" make findings of fact and conclusions of law in complex cases).

[12] Reeves Royalty Co., Ltd. v. ANB Pump Truck Serv., 513 So. 2d 595, 598-99 (Miss. 1987)(full faith and credit will not be given to foreign judgments procured by extrinsic fraud or misrepresentation).

[13] Mississippi Ass'n of Educators v. Trustees of the Jackson Mun. Separate School Dist., 510 So. 2d 123, 125 (Miss. 1987)(passage of legislation declaring strikes by public school teachers to be illegal rendered moot appeal from injunction prohibiting teacher strike); W & W Holdings, Inc. v. The Village at Henderson Point Owners' Ass'n, 503 So. 2d 286, 289 (Miss. 1987)(where hearing is required pursuant to Miss. R. Civ. P. 65(a), both sides must be allowed to present evidence before motion for preliminary injunction can be decided).

[14] Cooper v. City of Picayune v. Millbrook Property Owners Ass'n, 511 So. 2d 922, 923 (Miss. 1987)(circuit court sitting as appellate court has authority to allow interested third parties to intervene in appeal).

[15] Westmoreland v. Raper, 511 So. 2d 884, 884-85 (Miss. 1987)(Miss. R. Civ. P. 18 does not provide for joinder of insurer in direct action by third party on insurance policy); Ladner v. Quality Exploration Co., 505 So. 2d 288, 291-92 (Miss. 1987)(application of Miss. R. Civ. P. 19 to trespass action requires that, if possible, all persons with interest in subject property be joined as parties).

[16] Ward v. Foster, 517 So. 2d 513, 516-17 (Miss. 1987)(pursuant to Miss. R. Civ. P. 60(b)(5) final judgment may be modified by trial court even after appeal has been perfected); Rice Researchers, Inc. v. Hiter, 512 So. 2d 1259, 1265-66 (Miss. 1987)(although not recommended, absent clear abuse of discretion trial judge may adopt verbatim party's post-trial proposed findings of fact); Cox v. Howard, Weil, LaBouisse, Friedrichs, Inc., 512 So. 2d 897, 900-01 (Miss. 1987)(Miss. R. Civ. P. 54(b) final judgment upon multiple claims should only be granted on rare occasions; trial judge should set forth specific reasons for grant in his decision); Davis v. City of Lexington, 509 So. 2d 1049, 1051 (Miss. 1987)(trial judge errs in granting Miss. R. Civ. P. 12(b)(6) motion where necessary facts have yet to be developed).

[17] O'Neill v. O'Neill, 515 So. 2d 1208, 1211-12 (Miss. 1987)(motion to stay proceedings does not constitute appearance; defendant does not waive right to assert lack of personal jurisdiction); Read v. Sonat Offshore Drilling, Inc., 515 So. 2d 1229, 1230-31 (Miss. 1987)(foreign corporation qualified to do business in Mississippi subject to personal jurisdiction).

[18] Hutchins v. Page Contractors, Inc., 513 So. 2d 944, 945-46 (Miss. 1987)(question

verdicts,[19] relief from judgment,[20] remittitur,[21] sanctions,[22] service of process,[23] standing,[24] summary judgment,[25] supersedeas,[26] venue,[27] ver-

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of allowing jury view is discretionary with trial judge).

[19] Gill v. W.C. Fore Trucking, Inc., 511 So. 2d 496, 498 (Miss. 1987)(trial judge may reform improper jury verdict providing for apportionment among joint tortfeasores or order new trial; where new trial results in verdict for defendant, trial judge may not grant JNOV reinstating original result if unsupported by facts adduced at second trial).

[20] Fultz v. Doss, 507 So. 2d 891, 892 (Miss. 1987)(where final order of county court is at variance with original ruling, circuit court should reinstate original ruling; Miss. R. Civ. P. 60 provides that appellant has "reasonable time" to file motion for relief).

[21] Investors Property Management, Ltd. v. Watkins, Pitts, Hill & Assocs., 511 So. 2d 1379, 1381-82 (Miss. 1987)(order providing for remittitur but not new trial considered to be partial JNOV from which plaintiff may appeal).

[22] Selleck v. S.F. Cockrell Trucking, Inc., 517 So. 2d 558, 560 (Miss. 1987)(court may impose sanctions to protect integrity of its processes against party blatantly attempting to influence juror); Vicksburg Ref., Inc. v. Energy Resources, Ltd., 512 So. 2d 901, 902 (Miss. 1987)(courts may sanction attorneys who fail to properly schedule and notice motions, even absent bad faith, to protect integrity of judicial processes); White v. White, 509 So. 2d 205, 209 (Miss. 1987)(absent finding of willfulness or bad faith, trial judge abuses his discretion by dismissing noncomplying party's complaint pursuant to Miss. R. Civ. P. 37(b)(2)(C) where other party suffered no prejudice in its preparation for trial).

[23] Western Tar Prods., Inc. v. Alton Sheet Metal and Roofing Works, Inc., 515 So. 2d 932, 934-35 (Miss. 1987)(service of process requirements under abrogated Miss. R. Civ. P. 4); Pointer v. Huffman, 509 So. 2d 870, 873 (Miss. 1987)(constable may be delegated to serve process as special deputy pursuant to Miss. Code Ann. § 95-25-19 (1972); Breland v. Smith-Johnson, Inc., 501 So. 2d 389, 391 (Miss. 1987)(Miss. R. Civ. P.5(b) governs service of process upon party by intervenor).

[24] Canton Farm Equip., Inc. v. Richardson, 501 So. 2d 1098, 1107-10 (Miss. 1987)(private citizen has standing to maintain suit under Miss. Code Ann. §§ 19-13-37(1) and 31-7-57(2) & (3) to attack appropriation not authorized by law, and to assert any personal claims arising out of common nucleus of operative fact with statutory claims).

[25] Sherrod v. United States Fidelity and Guar. Co., 518 So. 2d 640, 644-45 (Miss. 1987) (ten-day notice requirement of Miss. R. Civ. P. 56(c) is "bright-line" test; however, harmless error analysis will be applied when requirement not met but non-moving party has not offered any evidence in support of his claim); Pope v. Schroeder, 512 So. 2d 905, 907-08 (Miss. 1987) (Miss. R. Civ. P. 56(c) requires motion for summary judgment to be served at least ten days before time fixed for hearing); Walker v. Cleveland Lumber Co., 512 So. 2d 695, 696 (Miss. 1987) (Miss. R. Civ. P. 12(b) motion to dismiss and Miss. R. Civ. P. 56 motion for summary judgment are interchangeable); Sumrall v. Doggett, 511 So. 2d 908, 910-11 (Miss. 1987) (summary judgment based upon affirmative defenses of estoppel or laches improper where defendant fails to meet burden of establishing these defenses and facts have not been fully developed); Gallagher v. Warden, 507 So. 2d 27, 29 (Miss. 1987) (in addition to following general case law in putting on proof of nonexistence of will, will contestant must also satisfy requirements of Miss. R. Civ. P. 56 by raising genuine issue of material fact sufficient to withstand motion for summary judgment); Shelton v. American Ins. Co., 507 So. 2d 894, 896-97 (Miss. 1987) (where terms of insurance contract are unambiguous in denying coverage for fraudulent acts of insured,

dicts,[28] and witnesses.[29]

I. INTERVENTION

The case of *Guaranty National Insurance Co. v. Pittman*[30] presented the Mississippi Supreme Court with its first opportunity to construe the requirements of Mississippi Rule of Civil Procedure 24(a)(2), Intervention of Right.[31] The action arose from a motor vehicle accident involving the plaintiff and a putative employee of a trucking company whose liability insurer was Guaranty National Insurance Co.[32] Following a default judgment taken against the truck driver,[33]

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insurer has no duty to defend suit against insured and summary judgment in favor of insurer on this issue is proper); Lester Eng'g Co. v. Richland Water and Sewer Dist., 504 So. 2d 1188, 1192 (Miss. 1987) (issue of existence of relationship of principal and agent is factual dispute inappropriate for resolution on motion for summary judgment); Brocato v. Mississippi Publishers Corp., 503 So. 2d 241, 243 (Miss. 1987)(ten-day notice requirement of MISS. CODE ANN. § 95-1-5 (1972) is necessary preliminary step to proper filing of libel action against publisher or broadcaster; although summary judgment is granted on improper grounds, it will be upheld if sufficient alternative grounds exist to support judgment below).

[26] McIntire v. Moore, 512 So. 2d 687, 689 (Miss. 1987) (decision to grant supersedeas discretionary with trial judge following appeal from commitment for chemical dependency treatment).

[27] H & W Transfer and Cartage Serv., Inc. v. Griffin, 511 So.2d 895, 901-02 (Miss. 1987) (objections to venue waived unless raised in answer or MISS. R. CIV. P. 12 motion).

[28] First Bank of Southwest Mississippi v. Bidwell, 501 So.2d 363, 366 (Miss. 1987) (Unlike FED. R. CIV. P. 49(b), MISS. R. CIV. P. 49(b) does not permit trial court to pose interrogatories in conjunction with general verdict).

[29] Salter v. Watkins, 513 So. 2d 569, 571 (Miss. 1987)(juror is not competent to testify concerning events which allegedly occurred during jury deliberations); Slay v. Illinois Cent. Gulf R.R. Co., 511 So.2d 875, 877 (Miss. 1987) (no error occurres where trial judge improperly denies party's request to call witness as adverse, but later permits extensive cross-examination of witness).

[30] 501 So.2d 377 (Miss. 1987).

[31] MISS. R. CIV. P. 24(a)(2) provides:

> (a) INTERVENTION OF RIGHT. Upon timely application, anyone shall be permitted to intervene in an action:
> (2) when the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter impair or impede his ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

Id.

[32] 501 So. 2d at 379. The defendant, Bobby Eugen Hardin, was driving a tractor and collided with another automobile, seriously injuring the plaintiff, Adrienne E. Pittman, a passenger in the other car. *Id.* GNIC was the liability carrier for Rail Water Transport, Ltd., under whose ICC permit Hardin was allegedly operating at the time of the acci-

GNIC unsuccessfully attempted to intervene and to have the default judgment vacated.[34]

On appeal, the supreme court held that the circuit court erred in refusing to allow GNIC to intervene,[35] but affirmed the denial of the motion to set aside default judgment.[36] The court began its analysis by observing that Rule 24(a)(2) provides four prerequisites that must be satisfied before a third party will be allowed to intervene.

> (1) he must make timely application;
> (2) he must have an interest in the subject matter of the action;
> (3) he must be so situated that disposition of the action may *as a practical matter* impair or impede his ability to protect his interest; and

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dent. *Id.* at 380.

[33] *Id.* at 379-80. Prior to the commencement of the action, Hardin received a letter from plaintiff's counsel advising him to refer the matter to his liability insurance carrier. Hardin took the letter to the president of his employer, Central States Terminals, Inc., and was ultimately advised that he was not covered by either Central or its liability insurance carrier. Suit was filed and Hardin was duly served with process; however, he neither answered the complaint nor appeared at trial, despite being notified by plaintiff's counsel that a default judgment would be taken against him if he failed to appear at trial. Upon application of plaintiff's counsel an entry of default was made by the clerk of the court at trial. The same day a final judgment on the default was entered, following a non-jury hearing which assessed Pittman's damages as $400,000.00. *Id.*

[34] *Id.* at 380. GNIC learned of the default judgment 20 days after its entry. Six months after the default judgment was taken, GNIC filed a motion for leave to intervene pursuant to Rule 24(a)(2) and a motion to set aside the default judgment. Both motions were denied by the circuit court. *Id.*

[35] *Id.* at 386.

[36] *Id.* at 386-89. Although the court allowed GNIC to intervene, it stressed that its rights were derivative. As such, the court stated that any argument that GNIC could make that the default judgment against Hardin should be vacated would be the same argument that Hardin could make. Although the court cautioned that default judgments are generally disfavored, it stated that the decision to vacate a default judgment lies within the sound discretion of the trial judge. *Id.* at 388. Confronted with Hardin's complete failure to defend the action, despite being warned by plaintiff's counsel of the consequences of failing to answer or defend, the court ruled that the circuit court did not abuse its discretion in refusing to set aside the default judgment. *Id.* at 389. Metaphorically addressing the impact of its decision, the court cautioned future litigants:

> It may be that people will miss fewer trains if they know the engineer will leave without them rather than delay even a few seconds. Although we are not about to inaugurate a policy of entering irrevocable defaults where no answer has been filed by the thirty-first day, we are equally resolved that people know that the duty to answer must be taken seriously. At some point the train must leave.

Id. at 388-89.

> (4) his interest must not already be adequately represented by existing parties.[37]

Addressing the question of timeliness, the court stated that although GNIC filed its motion for leave to intervene 140 days after entry of default, the concept of timeliness is not limited merely to the passage of time.[38] Additionally, the court observed that post-judgment intervention has been held to be timely in other jurisdictions.[39] Relying on a four-factor test developed by the United States Court of Appeals for the Fifth Circuit to determine whether a motion for leave to intervene is timely,[40] the court emphasized the fact that GNIC did not actually become aware of the existence of the action until three weeks after entry of default.[41] Balancing the divergent interests of the plaintiff and GNIC, the court held that the plaintiff would suffer no prejudice from GNIC's delayed intervention,[42] whereas GNIC would suffer "substantial prejudice" if the default judgment were undisturbed and it was subsequently found to be liable under the policy.[43] Finally, the court adopted precedent from other jurisdictions and held that the fact that the motion for leave to interment was filed after judgment was not so unusual a circumstance as to render it untimely.[44]

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[37] *Id.* at 381. Although the court stated that intervention must be allowed upon satisfaction of these four prerequisites, it observed that as a practical matter their wording was sufficiently broad to allow considerable exercise of judicial discretion in determining whether or not they had been satisfied. *Id.* at 381 n.1.

[38] *Id.* at 381.

[39] *Id. See* Hedges, Grant & Kaufmann v. United States, 762 F.2d 1299, 1302 (5th Cir. 1985) (post-judgment intervention allowed); Lawrence v. Burke, 431 P.2d 302, 310 (Ariz.Ct.App. 1967) (same).

[40] *Pittman*, 501 So. 2d at 382. *See* Hedges, Grant & Kaufmann v. United States, 762 F.2d 1299, 1302-03 (5th Cir. 1985); Stallworth v. Monsanto Co., 558 F.2d 257, 264-66 (5th Cir. 1977). The four factors developed by the Fifth Circuit are:

> (1) the length of time during which the would be intervenor actually knew or reasonably should have known of his interest in the case before the petitioned for leave to intervene;
>
> (2) the extent of the prejudice that the existing parties to the litigation may suffer as a result of the would be intervenor's failure to apply for intervention as soon as he actually knew or reasonably should have know of his interest in the case;
>
> (3) the extent of the prejudice that the would be intervenor may suffer if his petition for leave to intervene is denied; and
>
> (4) the existence of unusual circumstances militating either for or against a determination that the application is timely.

Pittman, 501 So. 2d at 382.

[41] *Pittman*, 501 So. 2d at 382.

[42] *Id.* The court observed that Hardin had filed a similar motion to vacate default one day prior to GNIC. Therefore, the delay Pittman would experience would be the same regardless of whether or not GNIC were allowed to intervene. *Id.*

[43] *Id.* at 383.

Having established that GNIC's motion for leave to interment was timely filed, the court considered whether GNIC had the requisite interest in the subject matter of the action to justify intervention.[45] Although other jurisdictions have held that insurer interests are "contingent" and insufficient to satisfy the interest requirement of Rule 24(a)(2),[46] the supreme court declined to adopt their reasoning. Instead, the court held that since GNIC was exposed to potential liability in the action as a result of the liability policy covering the defendant's putative employer, then it had an interest in the action sufficient to satisfy Rule 24(a)(2).[47] Addressing the third requirement for intervention of right, the practical disadvantage to the would-be intervenor if intervention is disallowed, the court observed that it is closely linked with the interest requirement.[48] The court held that GNIC satisfied the third requirement for intervention of right because it clearly would have been placed at a practical disadvantage in protecting its interest if it was not allowed to intervene.[49]

Finally, the court held that although the legal interests of GNIC and the defendant driver appeared to coincide, the defendant's clear inability to pay the judgment made it unlikely that he would maintain the action with the same vigor as GNIC.[50] Moreover, the defendant was suing GNIC in an action arising out of GNIC's handling of the instant case for $5,000,000.00 in actual and punitive damages.[51] Therefore, the court concluded that the fourth factor of the test was satisfied due to the clear inadequacy of representation of GNIC's interest by the defendant driver.[52] Since each of the four factors was satisfied, the court concluded that the circuit court had erred in denying GNIC's application to intervene as of right under Rule 24(a)(2).[53]

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[44] *Id. See supra* note 39 and accompanying text.

[45] *Pittman*, 501 So. 2d at 383. GNIC claimed to have the requisite interest in the subject matter of the action by virtue of the fact that it was the liability carrier for Rail Water Transport, Ltd., under whose ICC permit Hardin was allegedly operating at the time of the accident. *Id.*

[46] *See* Restor-A-Dent Dental Laboratories, Inc. v. Certified Alloy Prods., Inc., 725 F.2d 871, 874-76 (2d Cir. 1984) (insurer interests insufficient to meet interest requirement of Rule 24(a)(2)); J. MOORE, W. TAGGART & J. WICKER, MOORE'S FEDERAL PRACTICE, 24.07[2] (2d ed. 1985) (same).

[47] *Pittman*, 501 So. 2d at 384. The court stated, "[l]egalistic formalism and mechanical jurisprudence simply do not fit the language of the rule. All that is necessary is that GNIC establish an interest in the rights that are at issue in the litigation." *Id.*

[48] *Id.* The court rejected the argument that GNIC could adequately protect is interest by vigorous litigation in pending garnishment actions in federal court, relying on authority from other jurisdictions holding that the "mere availability of alternative forums is not sufficient to justify a denial of a motion to intervene." *Id.*

[49] *Id.* at 384-85.

[50] *Id.* at 385.

[51] *Id.* Hardin's action arose out of the GNIC's handling of the instant case. *Id.* The court stated that the mere existence of the suit indicated that there was a substantial

Addressing policy considerations, the court stated that Rule 24(a)(2) should be applied "to insure that litigation moves sensibly and purposefully forward."[54] To accomplish this goal, the court advocated a liberal attitude towards intervention, particularly where the intervenor is proceeding under Rule 24(a)(2).[55]

II. Service of Process

The Mississippi Supreme Court announced the requirements that must be satisfied to render an in personam judgment over a nonresident defendant in *Noble v. Noble*.[56] In an action to modify a final divorce decree,[57] the plaintiff attempted to effect service by publication and by mailing a copy of the publication by non-certified first class mail to the nonresident defendant. The chancery court declined to enter a monetary judgment against the defendant, ruling that it lacked in personam jurisdiction over him.[58]

On appeal, the court considered whether summons issued under Mississippi Rules of Civil Procedure 4(c)(4)(C)[59] is sufficient to confer

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conflict of interest between GNIC and Hardin and held that GNIC should not have to rely on Hardin to protect its interest. *Id*

[52] *Id.*

[53] *Id.* at 386.

[54] *Id.* at 385.

[55] *Id.* at 385-86. The court stated that a policy allowing liberal intervention could be tempered by the court's inherent power to control the intervenor's participation in the action, including the power to sever the intervenor's claims for pretrial or trial proceedings. *Id.* at 386.

[56] 502 So. 2d 317 (Miss. 1987).

[57] *Id.* at 318. Dorothy Noble filed for divorce, alimony and other relief on October 22, 1985. Summons was issued on her husband, Eli Noble, by nonresident publication. Additionally, a copy of the publication notice was mailed first class to Mr. Noble at his post office address in Columbia, South Carolina. Mr. Noble did not answer or appear. *Id.* The chancery court granted the divorce on January 31, 1986, but declined to award alimony, reasoning that due to ineffective service of process it lacked in personam jurisdiction over Mr. Noble to render a monetary judgment. *Id.* Mrs. Noble filed a motion to alter the final decree as to alimony on February 7, 1986, citing as error the court's determination that it lacked in personam jurisdiction over Mr. Noble. The motion was denied and Mrs. Noble appealed to the supreme court. *Id.*

[58] *Id.*

[59] *Id.* at 319. Miss. R. Civ. P. 4(c)(4)(A) & (C) provides:

in personam jurisdiction over a nonresident defendant for purposes of rendering a monetary judgment.[60] The court began its analysis by observing that Rule 4(c)(4)(C) is similar to the controlling pre-Rules statute under which in personam jurisdiction was not acquired over the defendant.[61] Thereafter, the court looked to the United States Supreme Court decision in *Kulko v. California Superior Court*,[62] which held that personal jurisdiction over a nonresident defendant can only be acquired through a showing of both reasonable notice to the defendant that the action has been brought[63] and sufficient connection between the defendant and the forum state.[64] Applying these standards, the court held that absent an appearance by the nonresident defendant, Rule 4(c)(4)(C) service of process alone is insufficient to confer in personam jurisdiction over a nonresident defendant for the purpose of

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> RULE 4. SUMMONS
> (c) SERVICE:
> (4) BY PUBLICATION
> (A) If the defendant in any proceeding in a chancery court, or in any proceeding in any other court where process by publication is authorized, by statute, be shown by sworn complaint or sworn petition, or by a filed affidavit, to be a nonresident of this state or not to be found therein on diligent inquiry and the post office address of such defendant be stated in the complaint, petition, or affidavit, or if it be stated in such sworn complaint or petition that the post office address of the defendant is not known to the plaintiff or petitioner after diligent inquiry, or if the affidavit be made by another for the plaintiff or petitioner, that such post office address is unknown to the affiant after diligent inquiry and he believes it is unknown to the plaintiff or petitioner after diligent inquiry by the plaintiff or petitioner, the clerk, upon filing the complaint or petition, account, or other commencement of a proceeding, shall promptly prepare and publish a summons to the defendant to appear and defend the suit. The summons shall be substantially in the form set forth in Form 1-C.
> (C) It shall be the duty of the clerk to hand the summons to the plaintiff or petitioner to be published, or, at his request, and at his expense, to hand it to the publisher of the proper newspaper for publication. Where the post office address of the absent defendant is stated, it shall be the duty of the clerk to send by mail (first class mail, postage prepaid) to the address of the defendant, at his post office, a copy of the summons and complaint and to note the fact of issuing the same and mailing the copy, on the general docket, and this shall be evidence of the summons having been mailed to the defendant.

MISS. R. CIV. P. 4(c)(4)(A) & (C).

[60] *Noble*, 502 So. 2d at 318.

[61] *Id.* at 319. The pre-Rules statute is codified at MISS. CODE ANN. § 13-3-19 (1972).

[62] 436 U.S. 84 (1978). *Kulko* stands for the proposition that state courts are limited by the Due Process Clause of the fourteenth amendment in their jurisdictional ability to enter judgments affecting the rights of nonresident defendants. *Id.* at 91.

[63] *Id.*

[64] *Id.*

rendering a monetary judgment against him because of the inadequacy of notice to him.[65]

Having decided that Rule 4(c)(4)(C) service of process is insufficient to confer in personam jurisdiction over a nonresident defendant, the court then addressed the issue of what would constitute sufficient service of process for conferring in personam jurisdiction over a nonresident defendant.[66] Mississippi Rule of Civil Procedure 4(c)(5)[67] provides that process may be served on a nonresident by sending a copy of the summons and complaint to the person to be served by certified mail, return receipt requested. The court held that compliance with Rule 4(c)(5) requirements, including the return receipt or the return of the envelope marked "Refused" and the establishment of a sufficient nexus between the nonresident defendant and Mississippi, would be sufficient to confer in personam jurisdiction over him.[68]

In a separate opinion, Justice Robertson concurred that Rule 4(c)(5) service of process was sufficient to confer in personam jurisdiction over a nonresident defendant, but argued that the same result should obtain under Rule 4(c)(4)(C) as well.[69] Justice Robertson opined that the court had rendered the defendant "a little bit pregnant" in that under its analysis, his marital rights could be radically affected while his monetary rights remained undisturbed.[70]

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[65] *Noble*, 502 So. 2d at 320. The court concluded that, "absent some proof of defendant's receipt of summons, the reasonableness of notice is questionable." *Id.*

[66] *Id.*

[67] MISS. R. CIV. P. 4(c)(5) provides:

> (5) *Alternative Service on Person Outside the State.* In addition to service by any other method provided by this rule, a summons may be served on a person outside this state by sending a copy of the summons and of the complaint to the person to be served by certified mail, return receipt requested. Where the defendant is a natural person, the envelope containing the summons and complaint shall be marked "restricted delivery." Service by this method shall be deemed complete as of the date of delivery as evidenced by the return receipt or by the returned envelope marked "Refused."

MISS. R. CIV. P. 4(c)(5).

[68] *Noble*, 502 So. 2d at 319-20.

[69] *Id.* at 321-22 (Robertson, J., concurring). Justice Roberston stated that the court was needlessly distinguishing between the defendant's rights regarding the marital res and his rights regarding his pocketbook, and argued that any distinction between in personam and in rem jurisdiction had been eliminated in Shaffer v. Heitner, 433 U.S. 186 (1977). *Noble*, 502 So. 2d at 321-22 (Robertson, J., concurring).

[70] *Noble*, 502 So. 2d. at 321.

III. Separation of Powers

Dye v. State ex rel. Hale[71] presented the court with the opportunity to delineate the constitutional limits of the powers of the Lieutenant Governor of the State of Mississippi. Two state Senators sought a declaratory judgment[72] that certain Senate Rules[73] violated the separation of powers provisions[74] of the Mississippi Constitution of 1890 in that they conferred unconstitutional legislative powers upon the Lieutenant Governor, a member of the executive branch.[75] The primary challenge concerned certain Senate Rules that grant the Lieutenant Governor almost plenary powers concerning appointment of committees and referral of bills to committees.[76] The circuit court held that the Lieutenant Governor was a member of the executive branch of government, that the challenged Senate Rules pertaining to appointment of committees and referral of bills to committees were unconstitutional, and that any exercise of the power conferred by those Rules by the Lieutenant Governor was a violation of the separation of powers provisions in the Mississippi Constitution.[77]

On appeal, the Mississippi Supreme Court began with an analysis of the preliminary procedural issues of subject matter jurisdiction, standing, justiciability of the claim, waiver and estoppel questions, and whether or not the plaintiffs had exhausted their legislative remedies.[78] Addressing the question of subject matter jurisdiction, the court rejected the Lieutenant Governor's argument that the suit was an improperly brought quo warranto action,[79] and held that the allegations in the complaint were sufficient to confer subject matter jurisdiction upon the circuit court.[80] Specifically, the court held that, if proven the allegations in the complaint to the effect that the Lieutenant Governor was exercising legislative powers in the Senate in violation of the separation of powers provisions of the Mississippi Constitution were sufficient to state a claim upon which relief could be granted.[81] Rejecting the argument that the Attorney General should have exclusive authority to bring suit,[82] the court held that the senators had standing to maintain the action because they were adversely affected by the "ongoing actions" of the Lieutenant Governor.[83]

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[71] 507 So. 2d 332 (Miss. 1987).

[72] *Id.* at 335. Senators Richard S. Hale and Gene Taylor filed suit in the Circuit Court of Hinds County on January 24, 1986. *Id.*

[73] *Id.* The Senators sought a declaratory judgment that Senate Rules 5, 6, 7, 17, 18, 19, 36, 37, 38, 48, 65, 74 and 75 violate the separation of powers provision enumerated in art. 1, §§ 1 and 2 of the Mississippi Constitution of 1890. The primary Rules challenged were Senate Rule 7, which empowers the Lieutenant Governor to nominate and select Senate committees and Senate Rule 74, which empowers the Lieutenant Governor to refer bills to committees. *Id.* at 335-36.

[74] *Id.* The Mississippi separation of powers provisions are set out in art. 1, §§ 1 and 2 of the Mississippi Constitution of 1890 which provide:

> Section One. The powers of the government of the State of Mississippi shall be divided into three distinct departments, and each of them confided to a separate magistracy, to-wit: those which are legislative to one, those which are judicial to another, and those which are executive to another.
>
> Section Two. No person or collection of persons, being one or belonging to one of these departments, shall exercise any power properly belonging to either of the others. The acceptance of an office in neither of these departments shall, of itself, and at once, vacate any and all offices held by the person so accepting in either of the other departments.

Miss. Const. art. 1, §§ 1 & 2.

[75] *Dye*, 507 So. 2d at 336. The Senators argued that the Senate Rules were an unconstitutional delegation of legislative powers to the Lieutenant Governor, a member of the executive branch of government. *Id.*

[76] *See supra* note 73.

[77] 507 So. 2d at 337. The circuit court held that Senate Rules 7, 36, 37, 38, 48, 74 and 75 were unconstitutional, but upheld Rules 5, 6, 17, 18, 19 and 65. *Id.*

Although acknowledging the general rule that it would decline to adjudicate political controversies,[84] particularly when they involve the internal affairs of another branch of the government, the court held that the claim did not present a non-justiciable political controversy.[85] The court reasoned that where a violation of the doctrine of separation of powers is alleged, the court has both the authority and the responsibility to decide the issue.[86] Additionally, the court observed that since the controversy was the subject of great public concern, then it was imperative that it be resolved.[87]

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[78] *Id.* at 337-40.

[79] *Id.* at 337. Although the court observed that the action was similar to quo warranto proceedings, the court held that MISS. CODE ANN. § 11-39-3 (1972), the statute prescribing the formalities of quo warranto writs, had been supplanted by the Mississippi Rules of Civil Procedure. *Dye*, 507 So. 2d at 337 n.4.

[80] *Id.* at 338.

[81] *Id.* The court stated that a complaint alleging a violation of the separation of powers doctrine stated a claim upon which relief could be granted. *Id.*

[82] *Id.* The court refused "to relegate to the Attorney General either the exclusive authority to bring . . . [suit] . . . or the discretion whether and how that authority should be exercised." *Id.*

[83] *Id.*

[84] *Id. See* Barnes v. Ladner, 241 Miss. 606, 616, 131 So. 2d 458, 461 (1961) (court will decline to adjudicate controversies arising from conduct of internal affairs within legislative department).

[85] *Dye*, 507 So. 2d at 338-39. The court averred that the legislature is not above the law. Accordingly, where the legislature is alleged to have contravened rights secured by the constitutions of the United States or Mississippi, the judiciary has the responsibility to adjudicate the claim. *Id.*

[86] *Id. See* Alexander v. State ex rel. Allain, 441 So. 2d 1329, 1333 (Miss. 1983) (court has authority to adjudicate claims arising from alleged violation of separation of powers).

The final preliminary matter considered by the court was the Lieutenant Governor's allegation that the Senators were precluded from bringing suit because they had waived any objections to the challenged Rules. Since the Rules were adopted without dissent while the plaintiffs were members of the Senate, the Lieutenant Governor argued that the Senators should be estopped from challenging their constitutionality.[88] However, the court rejected this argument, stating that should it be accepted it would enable the Constitution to be amended by waiver and estoppel.[89]

The court began its consideration of the merits of the case with an historical analysis of the office of the Lieutenant Governor.[90] The court observed that the Lieutenant Governorship was originally created in the Mississippi Constitution of 1869, which granted to that office the Presidency of the Senate, with the complementary rights to debate all questions on the floor of the Senate and to vote where necessary to break a tie.[91] In 1870, the Senate adopted rules that granted further privileges to the office, including the power to appoint committees.[92] During the constitutional convention of 1890, there was a strong movement to eliminate the office; however, it ultimately failed and the office was retained.[93] The court relied heavily on a 1912 revision of the Senate Rules which empowered the Lieutenant Governor to appoint the members of committees and refer bills to the committees to conclude that the legislative history of the Lieutenant Governorship shows that the framers of the Mississippi Constitution intended to confer broad powers upon the office.[94]

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[87] *Dye*, 507 So. 2d at 339.

[88] *Id.* The Lieutenant Governor relied on two quo warranto cases, State ex rel. Jordan v. Mayor & Comm'rs. of Greenwood, 157 Miss. 836, 129 So. 682 (1930) and State ex rel. Patterson v. Land, 231 Miss. 529, 95 So. 2d 764 (1957), in asserting his waiver and estoppel arguments. Additionally, he argued that the Senators had not exhausted their administrative remedies in that they should have proceeded under the Senate Rules which allow for the suspension of the Rules and the adoption of temporary Rules. *Dye*, 507 So. 2d at 339.

[89] *Id.* at 340. The court relied on *Alexander*, *supra* to make its determination. Additionally, the court declined to make exhaustion of non-judicial remedies a prerequisite to bringing the action. *Id.*

[90] *Id.* at 340-42. Art. V, § 128 of the Mississippi Constitution provides for the assistance of the office; sections 129 and 131 detail the powers of the office and provide for its quasi-legislative, quasi-executive existence. Section 129 provides:

> The lieutenant-governor shall, by virtue of his office, be president of the Senate. In committee of the whole he may debate all questions, and where there is an equal division in the Senate, or on a joint vote of both houses, he shall give the casting vote.

Miss. Const. art. V, § 129.

Section 131 provides in part:

> When the officer of governor shall become vacant, by death or otherwise, the lieutenant governor shall possess the powers and discharge the duties of said office. When the governor shall be absent for the state, or unable, from protracted illness, to perform the duties of the office, the lieutenant governor shall discharge the duties of said office until the governor be able to resume his duties;. . .

Miss. Const. art. V, § 131.

Addressing the precise issue of whether the exercise of the privileges conferred upon the Lieutenant Governor by the current Senate Rules constituted a violation of the doctrine of separation of powers, the court followed two canons of constitutional construction. First, the court stated that "constitutional provisions should be read so that each is given maximum effect and a meaning in harmony with that of each other."[95] The court stated that where conflict exists between specific provisions, such as between the specific grant of rulemaking authority to the senate[96] and the general prohibition against the violation of the doctrine of separation of powers,[97] the specific provisions should control.[98] Second, the court stated that the constitution should be read in such a way as to best serve the present interests and needs of the state.[99]

Having established these guidelines for interpretation, the court delineated three questions to be answered to resolve the controversy. First, the court addressed the question of whether or not the powers to appoint committees and refer bills to committees were inherent in the office of the President of the Senate.[100] Although concluding that these powers were properly reserved to the Senate itself,[101] the court refused to hold that they were inherent powers of the office of the President of the Senate.[102]

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[91] *Dye*, 507 So. 2d at 340.

[92] *Id.*

[93] *Id.* at 341. Delegate W.A. Boyd motioned to terminate the office of Lieutenant Governor, arguing that it was a "fifth wheel to the wagon of government." His motion initially passed 45 to 37 however, on motion to reconsider, the delegates voted 54 to 47 to retain the office. *Id.*

[94] *Id.* The court stated that the "Senate's Rules have historically interpreted the Lieutenant Governor's powers to include the selection of committees and the assignment of bills." *Id.*

[95] *Id.* at 342. *See* St. Louis & San Francisco Ry. Co. v. Benton County, 132 Miss. 325, 330, 96 So. 689, 690 (1923) (in order to deduce meaning of constitution it is necessary to construe it *in toto*).

[96] *Dye*, 507 So. 2d at 342. Art. IV, § 55 provides in pertinent part: "[e]ach house may determine rules of its own proceedings,. . ." MISS. CONST., art. IV, § 55.

[97] *See supra* note 74.

[98] *Dye*, 507 So. 2d at 342.

[99] *Id.*

Secondly, the court considered whether or not the Senate had the inherent power to determine how the disputed powers could be exercised.[103] Although the court recognized its own authority to declare Senate Rules unconstitutional,[104] it stressed that the Mississippi Constitution of 1890 conferred substantial authority upon the Senate to determine its procedural rules.[105] The court also relied on precedent to hold that procedural rules of the respective branches of government should not be overturned unless they are "manifestly" beyond the constitutional authority conferred.[106] Regarding the disputed Senate Rules, the court held that they unquestionably enabled the Senate to operate more efficiently.[107] Therefore, the court held that the conferral of power under those rules was a valid exercise of the Senate's procedural rulemaking authority.[108]

Third, the court considered whether those powers could be conferred upon the Lieutenant Governor.[109] Although the circuit court had held that conferring those powers upon the Lieutenant Governor violated the separation of powers doctrine,[110] the court pointed out that the doctrine does not have an existence separate from that defined in the constitution.[111] Accordingly, a violation of the doctrine can exist only where there is a corresponding or concurrent violation of constitutional mandates. Since the constitution specifically provides that the Lieutenant Governor is an officer in both the legislative and executive branches of government, of necessity he must wield power emanating from both branches. Because the constitution confers upon the Lieutenant Governor the Presidency of the Senate, the court stated that "[he] is enough of a member of the Senate to have conferred upon him the legislative powers granted by the rules . . . at issue"[112] Therefore, the court reversed the circuit court's ruling that the lieutenant governor's exercise of the senate conferred powers to appoint committees and refer bills to committees violated the separation of powers doctrine, and held that the Senate has the inherent authority to establish procedural rules regarding its governance and that the lieutenant governor, by virtue of being the President of the Senate, can constitutionally exercise the powers conferred upon him through the senate rules.

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[100] *Id.* at 344. The Lieutenant Governor argued that § 129 operated to inhere to the office of the Lieutenant Governor the powers of appointing committees and referring bills to committees. *Id.*

[101] *Id.*

[102] *Id.*

[103] *Id.* at 345-46.

[104] *Id.*

[105] *Id.* The court compared the Senate's authority to determine its own procedural rules with the court's authority to adopt procedural rules for the judiciary. *See* Newell v. State, 308 So. 2d 71, 76 (Miss. 1975) (inherent power of court to determine its own procedural rules emanates from constitutional concept of separation of powers). Additionally, the court stated that principles of comity required that it defer to the Senate's authority to determine its own procedural rules unless the determination was "manifestly beyond" the Senate's constitutional authority." *Dye*, 507 So. 2d at 345-46.

[106] *Dye*, 507 So. 2d at 345. *See* Witherspoon v. State ex rel. West, 138 Miss. 310, 324-26, 103 So. 134, 138-39 (1925) (Senate supreme in its own sphere; no other branch of government may interfere unless Senate is manifestly wrong).

[107] *Dye*, 507 So. 2d at 346. The court observed that the Senate as a whole could not efficiently appoint committees or refer bills; therefore, of necessity, it had to confer its authority on someone. *Id.*

[108] *Id. See supra* note 107.

[109] *Dye*, 507 So. 2d at 346-47.

In separate opinions, Justices Sullivan and Hawkins joined in dissenting from the majority decision.[113] Justice Sullivan termed the conferral of powers upon the Lieutenant Governor by the Senate Rules as effecting an unconstitutional transformation of that office from "Governor in Waiting" to "Overlord of the Senate."[114] Justice Sullivan argued that the scheduling of powers by the constitution should be presumed to be exclusive.[115] Accordingly, he believed the court erred in holding that the Senate could confer through its rules greater powers upon the Lieutenant Governor than those enumerated in the constitution.[116] Justice Sullivan believed that instead of engaging in historical analysis to determine the parameters of the office, the court should have looked solely to the language of the constitution.[117] Finally, Justice Sullivan strongly condemned the court's dilution of the potency of the constitution's mandate of separation of powers. Recognizing the force of the doctrine in federal law, he felt that its application in Mississippi was even more forceful because it was incorporated into the constitution itself.[118] Therefore, Justice Sullivan argued that when the separation of powers provision was given its intended effect, the exercise of power conferred upon the Lieutenant Governor by the Senate could only be seen as a clear violation of the doctrine.[119]

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[110] *Id.* at 346. *See supra* note 77.

[111] *Dye*, 507 So. 2d at 346. The court stated: "there is no natural law of separation of powers. Rather, the powers of government are separate only insofar as the Constitution makes them separate." *Id.* Additionally, the court observed that the constitution confers office and authority upon the Lieutenant Governor in both the legislative and executive branches of government. *Id. See supra* note 90 and accompanying text.

[112] *Dye*, 507 So. 2d at 346-47 *See supra* notes 90, 96 and accompanying text.

[113] *Dye*, 507 So. 2d at 348 (Sullivan, J., dissenting) (joined by Justice Hawkins); *Id.* at 358 (Hawkins, J., dissenting) (joined by Justice Sullivan).

[114] *Id.* at 351 (Sullivan, J., dissenting).

[115] *Id.* at 349. Justice Sullivan cited State ex rel. Greaves v. Henry, 87 Miss. 125, 40 So. 152, 154 (1904) to support this assertion. *Dye*, 507 So. 2d at 349.

[116] *Dye*, 507 So. 2d at 357. Justice Sullivan argued that the majority had expanded the words "[e]ach house may determine the rules of its own proceedings" into a constitutional grant that would allow the Senate "to create a Senator out of the whole cloth." *Id.*

Justice Hawkin's dissent echoed many of the concerns expressed by Justice Sullivan. Additionally, Justice Hawkins argued that the majority failed to satisfactorily explain exactly why the Lieutenant Governor was eligible to have legislative powers conferred upon him solely because he is President of the Senate or why the Senate had the inherent delegatory authority to confer legislative powers in the first place.[120] Justice Hawkins believed that the court's decision was an unwarranted exercise of judicial interpretation that ratified the creation of arbitrary power that denigrated the "grandeur of the constitution" and stripped the people of their voice in government.[121]

He also believed that since the people of Mississippi had delegated legislative powers to the Senate, the Senate could not in turn delegate them to the Lieutenant Governor without the consent of the people. *Id. See* Alcorn v. Hamer, 38 Miss. 652, 749 (1860) (legislature cannot surrender its authority without violating constitution).

[117] *Dye*, 507 So. 2d at 349. Justice Sullivan argued, "where the language of the constitution is plain, subsequent action by the departments of government are (sic) contemporaneous or antecedent history on the subject cannot be appealed to for interpretation." *Id.*

[118] *Id.* at 352-53. Justice Sullivan believed that the majority belittled the importance of §§ 1 and 2 and argued that the severe penalty for violating the separation of powers left no doubt that it is a "constitutional commandment of utmost importance." *Id.*

[119] *Id.* at 353. Justice Sullivan disagreed with the majority's conclusion that language in *Alexander*, *supra*, that characterized the separation of powers as a strict mandate with no exceptions was merely dicta. *Id.*

[120] *Id.* at 360-61 (Hawkins, J., dissenting). Justice Hawkins argued that it was ludicrous to suggest that merely because the constitution authorized the Lieutenant Governor to be titular head of the Senate that it also authorized the Senate to confer upon him vast legislative powers. *Id.* at 361 n.4. Justice Hawkins observed that, "[t]he same drafters wrote Sections 1 and 2 and knew that Section 129 was making certain specific exceptions to them. If they had intended more exceptions, especially of such monumental proportion, can anyone doubt they would have specifically stated them?" *Id.*

[121] *Id.* at 362. Justice Hawkins cited with approval the following observation of the United Stated Supreme Court in Jones v. Securities and Exch. Comm., 298 U.S. 1 (1936):

> Arbitrary power and the rule of the constitution cannot both exist. They are antagonistic and incompatible forces; and one or the other must of necessity

IV. FORUM NON CONVENIENS

Shewbrooks v. A.C. and S., Inc.[122] was the most controversial decision rendered in the area of civil procedure.[123] The action entailed a nonresident plaintiff seeking to recover for asbestos-related injuries against eighteen nonresident manufacturers of asbestos.[124] The plaintiff was proceeding in Mississippi because the statute of limitations had expired in every other jurisdiction in which he could have maintained the action.[125] The trial court dismissed the action, determining that it lacked personal jurisdiction over the defendants and applying the doctrine of *forum non conveniens*.[126] On August 19, 1987, the Mississippi Supreme Court handed down its intial decision in the action. Because the court was evenly divided 4-4,[127] the trial court's dismissal of the action based on the doctrine of *forum non conveniens* was upheld. While the petition for rehearing was pending, Chief Justice Walker retired from the court and was replaced by Justice Zuccaro. On rehearing, Justice Zuccaro sided with the original dissenters, resulting in the adoption of Justice Hawkins' August 19, 1987 dissent as the final

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> perish whenever they are brought into conflict.

298 U.S. at 24.

[122] No. 56,014 (Miss. Aug. 19, 1987), *rev'd on Reh'g*, 529 So. 2d 557 (Miss. 1988).

[123] *Compare:*

Thanks to the wisdom of this Court, the chance for the courts of this state to be one (sic) of the forerunners in this salutary development has been abandoned.
And thanks to the humanity of this Court, Mr. and Mrs. Shewbrooks in their one last opportunity to prove their claim, no matter how meritorious it may be, have had the courtroom door slammed in their faces.

No. 56,014, slip op. at 25 (Miss. Aug. 19, 1987) (Hawkins, J., dissenting)

with: "we have doomed Mississippi to become a dumping ground for the nation's homeless tort litigation." No. 56,014, slip op. at 1 (Miss. Aug. 19, 1987), *rev'd on rehearing*, 529 So. 2d 557 (Anderson, J., dissenting).

[124] *Shewbrooks*, 529 So. 2d at 559. Nevin and Anna Mae Shewbrooks filed suit in the Circuit Court of the First Judicial District of Hinds County against 18 nonresident corporate defendants, seeking damages for asbestos poisoning received by Mr. Shewbrooks in Delaware, Pennsylvania, and New Jersey as a result of the mining, manufacturing and distribution of asbestos by the various defendants. *Id.* The complaint charged the defendants with knowingly mining, manufacturing and marketing asbestos years after discovering its dangers and with wilfully concealing these dangers from their employees and the public. *Id.*

[125] *Id.* at 568 (Robertson, J., dissenting). The cause of action accrued in one of three states: Delaware, Pennsylvania, or New Jersey, each of which has a two-year statute of limitations. *Id.*

[126] *Id.* at 559.

[127] No. 56,014, slip op. at 10 (Miss. Aug. 19, 1987). Justice Anderson, joined by Justices Robertson, Prather, and Roy Noble Lee, authorized the opinion of the court. Justice Hawkins dissented, joined by Justices Sullivan, Griffin, and Dan Lee.

May 11, 1988 majority opinion. Because of the importance of the case, this comment will discuss the opinions written in both the initial 1987 and final 1988 decisions.

A. *The Initial Decision*

The original opinion in the action was authored by Justice Anderson. In that opinion, the court declined to address the trial court's determination that it could not exercise personal jurisdiction over the foreign corporations, assuming arguendo that personal jurisdiction existed.[128] Instead, the court focused on the *forum non conveniens* issue and determined that it afforded an independent ground for dismissal of Shewbrooks' claim.[129] The court defined the doctrine of *forum non conveniens* as a discretionary judicial device that allows a court to refuse to hear a case although it has the power to do so.[130] The court held that since *forum non conveniens* is discretionary with the trial judge, any determination he makes regarding the application of the doctrine should be afforded "substantial deference," and a dismissal based upon *forum non conveniens* should only be overturned where it is clear that the trial judge has abused his discretion.[131] The court held that the trial judge had not abused his discretion, stating that a foreign cause of action involving foreign plaintiffs suing foreign defendants did not belong in Mississippi courts.[132]

The court also dismissed Shewbrooks' argument that application of *forum non conveniens* was inconsistent with article III, section 24 of the Mississippi Constitution of 1890,[133] which states that Mississippi courts shall be open to every person who has suffered an injury. The court stated that section 24 is merely a general statement of policy that does not prevent the judiciary from setting reasonable standards for the operation of the courts.[134]

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[128] No. 56,014, slip op. at 2 (Miss. Aug. 19, 1987). The court also held that Mississippi's borrowing statute, Miss. Code Ann. § 15-1-65 (1972), did not apply because Shewbrooks did not move to Mississippi. No. 56,014, slip op. at 2-3 (Miss. Aug. 19, 1987).

[129] No. 56,014, slip op. at 2 (Miss. Aug. 19, 1987).

[130] *Id.* at 3-4. *See* NAACP v. Claiborne Hardware Co., 393 So. 2d 1290, 1294-95 (Miss. 1981) (recognition of doctrine of *forum non conveniens*), *rev'd on other grounds*, 458 U.S. 886 (1982); Illinois Cent. Gulf R.R. Co. v. Moore, 215 So. 2d 419, 421 (Miss. 1968) (same). Although recognizing that jurisdiction is the court's power to hear a suit, Justice Anderson distinguished between a grant of power and the use thereof: "[i]n a way, jurisdiction is like sex. Being able to do something does not determine whether you *should* do it." No. 56,014, slip op. at 4 (Miss. Aug. 19, 1987).

[131] No. 56,014, slip op. at 4 (Miss. Aug. 19, 1987).

[132] *Id.*

[133] Art. IV, § 24 provides:

> All courts shall be open and every person for any injury done him in his lands, goods, person or reputation shall gave a remedy by due course of law and right justice shall be administered without sale, denial or delay.

Miss. Const. art. IV, § 24.

Finally, the court rejected Shewbrooks' contention that *forum non conveniens* could not be applied because the defendants did not show the existence of an alternative forum in which the action could be maintained. The court held that *forum non conveniens* is applicable to any case where the defendants are merely "amenable to process;"[135] existence of another forum in which the claim may be litigated is not a prerequisite to the application of the doctrine.[136] Additionally, the court held that the trial court need not condition a dismissal based on *forum non conveniens* upon the defendant's agreeing to stipulate that it will make no objections as to lack of personal jurisdiction or expiration of the statute of limitations claims it may have in the alternative forum.[137]

In sum, the original *Shewbrooks* opinion advocated the increased usage of the doctrine of *forum non conveniens* by Mississippi trial courts as a way to rid the Mississippi judicial system of litigation that has no nexus with Mississippi and is only being brought in the state because of our favorable six-year tort statute of limitations.

B. *Justice Robertson's Opinion*

Justice Robertson advocated the application of Mississippi's center of gravity/choice of law rules to the case.[138] Although he believed that the application of *forum non conveniens* produced a sound result in this case, he preferred the choice of law analysis because he believed it would provide for a more just and uniform application of the law.[139] Although he believed that subject matter jurisdiction[140] and venue were both proper in Mississippi, he felt that Shewbrooks' claim should have been dismissed because the applicable statute of limitations had expired. While recognizing that Mississippi's borrowing statute[141] was inapplicable because Shewbrooks did not move to Mississippi, he felt that application of Mississippi's center of gravity/choice of law rules would produce the same result.

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[134] No. 56,014, slip op. at 5 (Miss. Aug. 19, 1987).

[135] No. 56,014, slip op. at 6 (Miss. Aug. 19, 1987). Justice Anderson, citing Gulf Oil Corp. v. Gilbert, 330 U.S. 501 (1946), asserted that the amenability to process in another forum, and not the ability to proceed on the merits in the other forum is the proper prerequisite to applying the doctrine of *forum non conveniens*. Justice Anderson relied heavily on Islamic Republic of Iran v. Pahlavi, 62 N.Y.2d 474, 467 N.E.2d 245 (1984). In *Islamic Republic*, the New York Court of Appeals affirmed the dismissal of a claim of the Republic of Iran against the deposed Shah. The court of appeals advocated the use of *forum non conveniens* as a method of controlling the judicial docket. 62 N.Y.2d at 478, 467 N.E.2d at 247. While recognizing that the availability of an alternative forum is a "most important factor," the court of appeals refused to hold that it is a prerequisite for applying the doctrine of *forum non conveniens*. 62 N.Y.2d at 481, 467 N.E.2d at 249.

[136] *See supra* note 135 and accompanying text.

[137] No. 56,014, slip op. at 8 (Miss. Aug. 19, 1987).

[138] *Shewbrooks*, 529 So. 2d at 568 (Robertson, J., dissenting). Justice Robertson's concurring opinion in the original hearing of the case and his dissenting opinion from the final decision were essentially identical.

Under Justice Robertson's analysis, the court should initially apply Mississippi's center of gravity/choice of law rules to determine which forum had the most significant relationship with the cause of action and the parties.[142] Following this determination, the court should then consider whether Mississippi had a substantial interest in the adjudication of the controversy that would mandate application of its statute of limitations.[143] Absent such an interest, the court should apply the statute of limitations applicable in the forum with the most significant relationship to the action and the parties.[144]

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[139] *Id.* at 573 (Robertson, J., dissenting). Justice Robertson advocated choice of law analysis as being the "modern trend" in this area of the law. Although he believed Justice Anderson's *forum non conveniens* argument was sound, he noted the existence of contrary authority in other jurisdictions. *Id.*

[140] *Id.*, at 568 n.1. Justice Robertson argued that there were serious problems with establishing that in personam jurisdiction existed over the nonresident defendants that neither did, nor qualified to do business in Mississippi. *Id.*

[141] Miss. Code Ann. § 15-1-65 provides:

> When a cause of action has accrued in some other state or in a foreign country, and by the law of such state or country, or of some other state and country where the defendant has resided before he resided in this state, an action thereon cannot be maintained by reason of lapse of time, then no action thereon shall be maintained in this state.

Miss. Code Ann. § 15-1-65 (1972). Although Justice Robertson acknowledged that Miss. Code Ann. § 15-1-65 (1972) was inapplicable, he argued that the underlying the statute is the principle that actions brought in Mississippi which should have properly been brought in another jurisdiction should be controlled by the statute of limitations in that other jurisdiction. *Shewbrooks*, 529 So. 2d at 570. (Robertson, J. dissenting).

[142] *Shewbrooks*, 529 So. 2d at 570-71 (Robertson, J., dissenting). Mississippi adopted the Restatement (Second) of Conflict of Laws analysis in tort cases in Mitchell v. Craft, 211 So. 2d 509, 515-16 (Miss. 1968). Section 145 of the Restatement provides:

> § 145. The General Principle
>
> (1) The rights and liabilities of the parties with respect of an issue in tort are determined by the local law of the state which, as to that issue, has the most significant relationship to the occurrence and the parties under the principles stated in § 6.

Restatement (Second) of Conflict of Laws § 145 (1971).

[143] *Shewbrooks*, 529 So. 2d at 571 (Robertson, J., dissenting).

C. *The Final Decision*

The final decision of the court, authored by Justice Hawkins, was essentially identical to his dissent from the court's original disposition of the case.[145] In that decision, the court embraced a judicial philosophy diametrically opposed with that of the initial ruling. While the initial ruling advocated the liberal use of *forum non conveniens* as a means to regulate court dockets,[146] the final decision maintained that the judiciary is a passive branch of government.[147] As such, the court held that any suit properly before the court must be heard.[148] The court emphatically stated that any distinction regarding access to Mississippi's courts between in-state and out-of-state citizens violated the privileges and immunities clause of article IV, section 2 of the United States Constitution.[149] Accordingly, the court held that Shewbrooks' claim must be heard.[150]

Addressing the application of *forum non conveniens*, the court stated that while it is an important qualification to the principles announced, there are certain circumstances in which it may not be applied.[151] Specifically, the court held that *forum non conveniens* may not be applied where there is no alternative forum in which to bring suit because its application would completely bar a plaintiff from bringing his claim.[152] Discussing the New York decision relied on so heavily by the initial decision, *Islamic Republic v. Pahlavi*,[153] the court concluded that there were four significant factors that distinguished that case:

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[144] *Id.*

[145] No. 56,014 (May 11, 1988). Shewbrooks v. A. C. and S. Inc., 529 So. 2d at 557 (Miss. 1988).

[146] *See supra* notes 123, 130, 135 and accompanying text.

[147] *Shewbrooks*, 529 So. 2d at 560.

[148] *Id. See* Knox County v. Aspinwall, 65 U.S. 376, 385 (1861) (federal court with proper jurisdiction is not justified in refusing to hear action); Cohens v. Virginia, 19 U.S. 264, 404 (1821) (treason to Constitution for federal court to decline to hear case properly before it).

[149] *Shewbrooks*, 529 So. 2d at 561. *See* Chambers v. Baltimore & O. Ry. Co., 207 U.S. 142, 149 (1907) (state law which affords citizens right to maintain action but denied right to citizens of other states is unconstitutional).

[150] *Shewbrooks*, 529 So. 2d at 559.

[151] *Id.* at 561-64.

[152] *Id.* at 561. *See* Zurick v. Inman, 426 S.E.2d 767, 771 (Tenn. 1968) (*forum non conveniens* presupposes that alternative forum exists where plaintiff may bring his suit).

[153] *See supra* note 135 and accompanying text.

> (1) *Islamic Republic* involved foreigners exclusively. The privileges and immunities clause of the United States Constitution was not affected;
> (2) the *Islamic Republic* court doubted if it had the power to afford complete relief, of which there was no doubt in *Shewbrooks*;
> (3) if the plaintiff could not get judicial relief under the judicial system of Iran, it was the plaintiff's own fault;
> (4) there was no statute of limitations involved in *Islamic Republic*.[154]

Furthermore, the court cited *Mcleod v. Lovelace*,[155] a subsequent New York case, and stated that *Mcleod* clearly showed that the New York court would not have applied the rationale of *Islamic Republic* to *Shewbrooks*.

Addressing the statute of limitations problem, the court held that *forum non conveniens* cannot be applied where the plaintiff's claim is barred elsewhere by a statute of limitations, unless the defendant agrees to waive his statute of limitations defense.[156] Rejecting Justice Robertson's choice of law analysis, the court held that since suit was properly brought in Mississippi, the Mississippi six-year statute of limitations was the proper statute of limitations to apply.[157] The court stated that the creation of statutes of limitations is a function of the legislative, not the judicial, branch of government.[158] Analyzing Mississippi's statutes of limitations, the court found that Mississippi's borrowing statute[159] clearly did not apply. Furthermore, the court held that since the legislature had reenacted that statute unchanged over the years, the court was interpreting the statute precisely as it should be interpreted.[160] Therefore, the court held that the proper statute to be applied was Mississippi's six-year statute, rendering Shewbrooks' claim timely brought in Mississippi. The court recognized that several respected academic authorities argued against application of the forum state's statute of limitations in this circumstance.[161] However, the court held that since the application of statutes of limitations was a matter of public policy, it was a question for the legislature, and not the courts, to address.[162]

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[154] *Shewbrooks*, 529 So. 2d at 563-64.

[155] 499 N.Y.S.2d 290 (N.Y. App. Div. 1986). In *Mcleod*, the New York Supreme Court (the court immediately below the court of appeals), affirmed the *forum non conveniens* dismissal of a suit arising from an auto accident that occurred in New York between two Canadian motorists. However, the supreme court conditioned the dismissal upon the defendant's agreeing to waive any statute of limitations defense he might have in the Canadian courts. *Id.* at 291.

[156] *Shewbrooks*, 529 So. 2d at 562-64. The court observed that 14 states require the defendant to waive any statute of limitations defenses he may have as a prerequisite to dismissing a case for *forum non conveniens. Id. See, e.g.* Torrijas v. Midwest Steel Erection Co., 474 N.E.2d 1250, 1255 (Ill. App. Ct. 1985) (dismissal based on *forum non conveniens* conditioned on defendant's waive of statute of limitations defense).

[157] *Shewbrooks*, 529 So. 2d at 566-68. The court observed that the common law in 18 states holds that the state will apply its own statute of limitations to suits brought therein. *See, e.g.* Crites v. Delta Airlines, Inc., 341 S.E.2d 264, 265-66 (Ga. Ct. App. 1986); Lee v. Estate of Cain, 476 N.E.2d 922, 924 (Ind. Ct. App. 1985); Clark v. Figge, 181 N.W.2d 211, 215 (Iowa 1971). Mississippi has upheld this rule in a long line of cases. *See, e.g.* Cowan v. Ford Motor Co., 437 So. 2d 46, 47 (Miss. 1986); Vick v. Cochran, 316 So. 2d 242, 246 (Miss. 1975); Guthrie v. Merchants Nat'l Bank of Mobile, 254 Miss. 532, 180 So. 2d 309 (1965).

[158] *Shewbrooks*, 529 So. 2d at 568.

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[159] *Id.* at 565-66. Aside from the facts, this was the only point upon which all members of the court agreed. *See supra* notes 128, 141 and accompanying text.

[160] *Shewbrooks*, 529 So. 2d at 566.

[161] *Id.* at 567-68. *See, e.g.* RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971), § 142 (amended 1987); Grossman, *Statutes of Limitation and the Conflict of Laws: Modern Analysis*, 1980 ARIZ. ST. L.J. 1 *passim*; Leflar, *The New Conflicts-Limitations Act*, 35 MERCER L. REV. 461 *passim* (1984).

[162] *Shewbrooks*, 529 So. 2d at 568.

CORPORATE, CONTRACT AND COMMERCIAL LAW

Great strides were made in the development of commercial law in the State of Mississippi, as the 1987 Mississippi Supreme Court addressed a multitude of legal issues arising out of disputes involving commerce or banking. The court resolved disputes concerning: the breach of a safe deposit box agreement;[1] contracts for employment,[2] retention of collateral by a secured party,[3] allegedly usurious loans,[4] actions by payees against banks for dishonoring checks,[5] personal liability under a continuing guaranty agreement,[6] security of renewed future advances by original collateral,[7] negotiable instruments,[8] action for wrongfully debiting a bank account,[9] claim of violation of the Federal Truth in Lending Act in relation to an agricultural loan,[10] duty of contractors to coordinate work at construction site,[11] breach of a hospital management contract,[12] breach of an agricultural lease contract,[13]

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[1] First Bank of Southwest Mississippi v. Bidwell, 501 So. 2d 363, 366 (Miss. 1987)(court upheld granting of peremptory instruction to effect that bank had breached its contractual agreement in allowing someone other than joint tenants to enter safe deposit box)(remanded for retrial on damages only).

[2] Perry v. Sears, Roebuck & Co., 508 So. 2d 1086, 1089 (Miss. 1987)(where no written contract of employment exist then employment may be terminated by either party at will; Mississippi recognizes neither implied covenant of good faith nor public policy exception to common law at-will termination rule); Fuselier, Ott & McKee, P.A., v. Moeller, 507 So. 2d 63, 67-68 (Miss. 1987)(where employer breaches employment contract providing for sixty days written notice before termination of employment, damages properly include two months salary and accrued vacation time, mitigated by salary actually paid to the employee following termination); Bruner v. University of S. Mississippi, 501 So. 2d 1113, 1116 (Miss. 1987)(valid employment contract cannot exist between university and individual absent nomination by school's president and approval by Board of Trustees of State Institutions of Higher Learning); Sloan v. Taylor Mach. Co., 501 So. 2d 409, 410-11 (Miss. 1987)(employee handbook not written contract of employment; where written contract allegedly exists but is so indefinite that parol evidence must complete its terms then contract is treated as oral one and one year statute of limitations controls).

[3] Millican v. Turner, 503 So. 2d 289, 292 (Miss. 1987)(Miss. Code Ann. § 79-9-505(2) (1972) will be interpreted so that creditor, who repossesses collateral which secures debt and retains that collateral for unreasonably long period of time without disposing of it, will be deemed to have elected to retain collateral in satisfaction of debt which it secures thus discharging debtor's obligation)(reasonableness is question of fact; remanded for trial as to reasonableness).

[4] Galloway v. Travelers Ins. Co., 515 So. 2d 678, 681 (Miss. 1987)(when individual, acting in furtherance of profit oriented business ventures, forms shell corporation in order to obtain loan which by its terms would be usurious if made to individual, transaction is not usurious if proceeds are used for business purpose); Benoit v. United Cos. Mortgage of Mississippi, Inc. 504 So. 2d 196 (Miss. 1987)(where loan governed by Small Loan Regulatory Act is, prior to its maturity, paid in full to creditor who is licensee under Small Loan Privilege Tax Act, then prepayment sought is calculated using "sum of the digits" method and to extent that general usury statute conflicts with this computation, usury statute is without effect).

[5] Deposit Guar. Nat'l Bank v. B.N. Simrall & Sons, Inc., 524 So. 2d 295, 299-300 (Miss. 1987)(where bank's debtor maintains general demand account with bank and said

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account receives funds solely in form of general deposits, then bank may set off funds of account against debts presently due from debtor to bank; third party payee who later presents his draft for payment from this account and finds the account insufficient to meet draft has no cause of action against bank); Central Bank of Mississippi v. Butler, 517 So. 2d 507, 510-11 (Miss. 1987)(where bank uses funds held in trust for benefits of holders of checks which draw on custodial account which contains trust funds to offset debt owed bank by separate and distinct entity, then holders of any dishonored checks written on trust account may maintain action against bank for improperly transferring trust funds).

[6] Hardy v. First Nat'l Bank of Vicksburg, 505 So. 2d 1021, 1023 (Miss. 1987)(where guaranty agreement provides for extinguishment of personal liability on note if principal owed on note is reduced according to agreement between parties, personal liability remains following foreclosure sale of property securing note because such sale does not constitute agreed upon reduction of principal).

[7] Cochran v. Deposit Guar. Nat'l Bank, 509 So. 2d 1045, 1046-47 (Miss. 1987)(holder of deed of trust securing indebtedness may foreclose upon default notwithstanding prior renewal of indebtedness by one other than grantor of deed of trust).

[8] Estate of Isaacson v. Isaacson, 508 So. 2d 1131, 1133-34 (Miss. 1987)(where certificates of deposit do not contain language "pay to the order of" or "to bearer" and by terms prohibit transfer, then such certificates are not negotiable instruments).

[9] Southern Seed Serv. of Greenville, Inc. v. Federal Deposit Ins. Corp., 516 So. 2d 472, 474 (Miss. 1987)(doctrine of estoppel will prevent maintenance of suit by bank customer for wrongful debiting of his bank account where customer by his conduct has ratified such debiting on previous occasions).

[10] Gregory v. Federal Land Bank, 515 So. 2d 1200, 1203 (Miss. 1987)(prior to March 31, 1980 credit transactions primarily for agricultural purposes in which total amount to be financed exceeded $25,000.00 were exempt from Federal Truth in Lending Act; where loan was executed prior to this date and was primarily for refinancing preexisting agricultural loans, then refinance loan is deemed to be primarily for agricultural purposes and exempt from federal act).

[11] CIG Contractors, Inc. v. State Bldg. Comm'n, 510 So. 2d 510, 512 (Miss. 1987)(where contract between state and its contractors specifically provides that contractors must coordinate work among themselves, no implied in law duty not to hinder or delay or to coordinate has been created).

[12] UHS-Qualicare, Inc. v. Gulf Coast Community Hosp., Inc., 525 So. 2d 746, 756-57 (Miss. 1987) (absent clear language to contrary, principle of material breach shall be implied at law in contracts when courts are called upon to interpret contract provisions that allow one party to terminate contract for technical breach of another party).

[13] Leard v. Breland, 514 So. 2d 778, 784 (Miss. 1987)(although in case of croplands, measure of damages for breach of lease contract by lessor is usually difference between value of crop immediately before and just after damage, less expenses saved, if there is no proof of expenses saved then proper award is amount of expenses incurred to raise

breach of a covenant not to compete,[14] availability of equitable remedy of quantum meruit,[15] use of contract actions by a labor union to enforce fines imposed on its members,[16] fraud in consumer transactions,[17] application of implied warranty of merchantability to used goods,[18] breach of service contract by telephone company,[19] propriety of state court hearing breach of natural gas sales contract claim prior to action by the Federal Energy Regulatory Commission,[20] ability of one mem-

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crop up to point of destruction only).

[14] Cooper v. Gidden, 515 So. 2d 900, 905 (Miss. 1987)(noncompetitive agreement between vendor and vendee of business will be construed as general agreement subject to assignment and transfer unless there is restrictive language in agreement showing it to be personal, flowing only to original vendee)(noncompetitive agreements protecting goodwill of business made between vendor and vendee will not be scrutinized for reasonableness as to time and space as closely as similar covenants between employers and employees).

[15] Estate of Johnson v. Adkins, 513 So. 2d 922, 925-26 (Miss. 1987)(where oral agreement to make devise is not adhered to, claimant with reasonable expectation of being compensated for value given may recover from estate on basis of quantum meruit); Estate of Van Ryan v. McMurtray, 505 So. 2d 1015, 1019 (Miss. 1987)(party who willfully violates fiduciary relationship comes into court with unclean hands and is not entitled to equitable remedy of quantum meruit).

[16] Communication Workers of America, Local 10517 v. Gann, 510 So. 2d 781, 783 (Miss. 1987)(absent fine schedule contained in constitution of union, which lists maximum fine to which union member will be subjected, union may not claim fines constitute contractual obligation nor may it pursue contractual remedy in Mississippi courts).

[17] Beck Enters., Inc. v. Hester, 512 So. 2d 672, 675 (Miss. 1987)(successfully proven case of fraud in consumer transaction enables plaintiff to choose between common law and Uniform Commercial Code remedies).

[18] Beck Enters., Inc. v. Hester, 512 So. 2d 672, 675-76 (Miss. 1987)(implied warranty of merchantability applies to both new and used goods); Hargett v. Midas Int'l Corp., 508 So. 2d 663, 664-65 (Miss. 1987)(implied warranty of merchantability applied to new and used goods; manufacturer fits the Uniform Commercial Code definition of "seller" and is subject to implied warranty of merchantability even though he is not in privity with purchaser of used goods).

[19] South Cent. Bell v. Epps, 509 So. 2d 886, 891 (Miss. 1987)(phone company has contractual relationship with subscribers to service; contract is breached upon erroneous disconnection of service)(compensatory damages for mental distress and hospitalization, secondary to breach of contract, are recoverable where it was foreseeable that termination would result in mental and physical illness; punitive damages, however, are not recoverable where breach was caused by mere inefficient recordkeeping).

[20] Southern Natural Gas Co. v. Fritz, 523 So. 2d 12, 17 (Miss. 1987)(where federal regulatory agency with primary jurisdiction over important but limited issue is involved in case presently before state trial court and has refused or failed to resolve that issue over four-year period, then trial court may resolve issue and need not stay its proceedings in favor of federal agency). The issue over which the federal agency had primary jurisdiction was whether an amendment to a natural gas sales contract which increased the price paid for deregulated gas produced under the contract was merely a device to

ber of a joint venture to contractually bind the venture,[21] availability of defense of lack of capacity to contract to one who contracts with a corporation while the latter is suspended for a failure to pay taxes,[22] recovery of loss of future net profits,[23] availability of defense of substantial performance,[24] presumption arising from contract language which recites an exchange of consideration,[25] principle of mutual consent in contract formulation,[26] and general principles concerning contract interpretation.[27]

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hide compensation in reality being exchanged for the sale of regulated gas subject to price ceilings under another contract — a violation of 18 C.F.R. § 270.207 (1988). *Southern Natural Gas*, 523 So. 2d at 14. The Mississippi Supreme Court held that a 1979 contract amendment did not violate federal regulations since the amendment was entered into prior to promulgation of the federal regulation and had the effect of increasing the sales price of deregulated gas not yet produced at the time of the amendment. *Id.* at 15-16 (distinguishing Columbus Gas Transmission Corp., 22 FERC ¶ 63,093 (1983) involving an agreement entered into after promulgation of the regulation and increased existing deregulated price on gas already being produced which FERC held to be an improper concealment of compensation for regulated gas).

[21] Jim Murphy & Assoc., Inc. v. LeBleu, 511 So. 2d 886, 891-92 (Miss. 1987)(one party to joint venture may execute contract with third party that is legally binding on other party to joint venture).

[22] Bryant Const. Co. v. Cook Constr. Co., 518 So. 2d 625, 631-32 (Miss. 1987) (when corporation enters into agreement during suspension under MISS. CODE ANN. § 37-13-27, such conduct is *ultra vires*; however, if the other contracting party breached and benefitted from contract, then *ultra vires* is no defense to breach and suspended corporation may bring suit after being reinstated to corporate status).

[23] Lovett v. E.L. Garner, Inc., 511 So. 2d 1346, 1353 (Miss. 1987) (one may recover for loss of future net profits in breach of contract case so long as such profits are proven with reasonable certainty and not based on speculation or conjecture).

[24] Board of Trustees of State Insts. of Higher Learning v. Johnson, 507 So. 2d 887, 888-89 (Miss. 1987) (when medical student, who obtained loan from Board for educational expenses in exchange for agreement to work in small community for five years and train in certain medical areas, fails to train in these areas and in bad faith actively conceals fact from Board, then student cannot avail himself of substantial performance doctrine).

[25] Daniel v. The Snowdoun Ass'n 513 So. 2d 946, 950 (Miss. 1987) (where contract contains recital of consideration, rebuttable presumption is created which requires party asserting lack of consideration to establish rebuttal by clear preponderance of evidence).

[26] Nunley v. Merrill, 513 So. 2d 582, 586 (Miss. 1987) (in order to create binding insurance contract there must be "a meeting of the minds" between insurer and insured).

[27] Cherry v. Anthony, Gibbs, Sage, 501 So. 2d 416, 419 (Miss. 1987) (viewing contract as whole, and absent clearly ambiguous contractual provisions, specific language will dictate intent of parties).

I. General Contract Principles

A. *Implied Requirement of Material Breach*

Contracts often contain provisions which delineate what conduct or omissions constitute a breach of contract giving the nonbreaching party a right to terminate the contract.[28] It is equally true that occasionally these provisions do not require that the conduct or omission amount to a material breach in order to justify contract termination; instead these provisions allow termination for conduct or omissions constituting a mere technical breach.[29] In 1987, the Mississippi Supreme Court held that unless the parties, by clear contractual language, expressly agree that termination can result from a technical breach then such provisions shall have implied into them the principle of material breach and termination can only result if:

> [there] is a failure to perform a substantial part of the contract or one or more of its essential terms or conditions, or if there is such a breach as substantially defeats its purpose . . . or when the breach of the contract is such that upon a reasonable construction of the contract, it is shown that the parties considered the breach as vital to the existence of the contract.[30]

This ruling was announced in *UHS-Qualicare, Inc. v. Gulf Coast Community Hospital, Inc.*,[31] a case involving a complicated factual situation wherein a joint venture sought to terminate a hospital management contract between the joint venture and one member of the joint venture.[32] At the time of the breach of contract, the joint venture Gulf

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[28] *See, e.g.*, UHS-Qualicare, Inc. v. Gulf Coast Community Hospital, 525 So. 2d 746, 748 (Miss. 1987) (once breach occurred, contract provided for termination at will of one party after notice to breaching party).

[29] *Id.* at 756.

[30] *Id.* (citing Gulf South Capital Corp. v. Brown, 183 So. 2d 802, 805 (Miss. 1966) and Matheney v. McClain, 248 Miss. 842, 849, 161 So. 2d 516, 520 (1964)).

[31] 525 So. 2d 746 (Miss. 1987).

[32] *UHS-Qualicare*, 525 So. 2d at 751. Gulf Coast Community Hospital, established in 1976, was financed and built by Safecare Company, Inc. (Safecare). In 1980, a joint venture was formed between Safecare and Qualicare of Louisiana, Inc. (Qualicare). As part of this venture each party took a 50% interest in Gulf Coast Community Hospital, Inc. (Gulf Coast, Inc.). At the same time, Gulf Coast, Inc. entered into a twenty-year management contract with Qualicare. In 1983, Qualicare was acquired by United Health Services, Inc. (UHS) and transferred all its interest in Gulf Coast, Inc. and assigned all of its rights and obligations under the management contract to UHS. UHS formed a subsidiary corporation, UHS-Qualicare, Inc. (UHS-Qualicare), to serve as the vehicle through which the acquisition took place. UHS-Qualicare became owner of fifty percent of the stock of Gulf Coast, Inc. and succeeded to Qualicare's position as manager of Gulf

Coast Community Hospital, Inc., consisted of Safecare Company, Inc. and UHS-Qualicare, Inc.[33]

The contract in question covered a term of twenty years and under its terms the joint venture reserved the right to approve the hospital budget or modifications thereof and to make all management and policy decisions, specifically including the right to set admission policies and fee structures.[34] The contract also provided that if UHS-Qualicare, as manager, failed to perform some duty or observe some limit imposed on it by the contract, and if such default continued thirty days after written notice from Gulf Coast, Inc., then after the expiration of that time period the contract terminated upon the giving of a second written notice.[35]

Subsequently, in June of 1983, UHS-Qualicare, acting as manager, increased the rates charged patients and modified the hospital's budget.[36] On June 16, 1983, Safecare wrote to UHS-Qualicare's parent corporation[37] complaining about the lack of consultation with respect to the change in rates.[38] After some boardroom maneuverings, the Board of Directors of Gulf Coast, Inc. came under the control of persons loyal to Safecare.[39] This same day, July 12, 1983, in a letter addressed to the parent corporation and UHS-Qualicare, Gulf Coast, Inc., through its newly elected board, declared the management contract terminated.[40] The letter generally focused on the changes in the hospital's fee structure and made no reference to the thirty day notice provision of the contract but did allege that the changes in the operation of the hospital were "materially detrimental."[41] However, at no time after this letter did Gulf Coast, Inc. reinstate the original fee structure or seek to countermand any of UHS-Qualicare's changes.[42]

On August 15, 1983, Gulf Coast, Inc. again announced termination of the contract and the following day filed suit against UHS-Qualicare and others[43] in circuit court,[44] seeking a declaratory judgment that the

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Coast Community Hospital.

[33] *Id.* at 748.

[34] *Id.* at 747-48.

[35] *Id.*

[36] *Id.* at 748.

[37] *Id.* UHS was the parent corporation. *See supra* note 32.

[38] *UHS-Qualicare*, 525 So. 2d at 748.

[39] *Id.* at 749.

[40] *Id.*

[41] *Id.* at 749-50.

[42] *Id.* at 750-51.

[43] *Id.* at 751-52. The suit named as defendants UHS-Qualicare, Inc., UHS and Qualicare. *Id.*

[44] *Id.* Suit was filed in the Circuit Court of Harrison County, Mississippi. *Id.*

contract had been breached by UHS-Qualicare and had been effectively terminated by Gulf Coast, Inc.[45] UHS-Qualicare answered and filed a counterclaim, joining as counter-defendants Safecare and certain others, and alleged, inter alia, the tortious interference with the management contract.[46] After a bench trial, the circuit court found that the changing of the fees and budget by UHS-Qualicare materially and substantially breached the management contract with Gulf Coast, Inc.[47] Furthermore, the trial court found that Gulf Coast, Inc. had effectively complied with the notice and opportunity for cure provisions of the contract.[48] Thereafter the lower court entered a declaratory judgment in favor of Gulf Coast, Inc. and dismissed UHS-Qualicare's counterclaim.[49]

On appeal, the Mississippi Supreme Court held that the circuit court erred in determining that the fee and budget changes made by UHS-Qualicare amount to a material breach of contract.[50] Initially, the court declared that a contract provision which delineates what conduct or omission constitutes a breach giving rise to termination of the contract should have implied into it the concept of material breach unless the contract clearly and unambiguously provides that a technical breach shall give rise to termination.[51] Next, the court recognized that UHS-Qualicare had technically breached the contract by changing the fees and budget of the hospital, a right reserved to Gulf Coast, Inc., but that the breach was not material since Gulf Coast, Inc. had total and absolute authority to immediately undo the breach and its effect.[52] Noting that the termination of a contract is a drastic remedy available only for a material breach and the general rule that a party may not take advantage of its own acts or omissions, the court held that Gulf Coast, Inc. could not declare termination of the contract when it could undo the breach by simply directing UHS-Qualicare to return to the previous budget and fees structure.[53] In this regard, the court stated that if Gulf Coast, Inc. had given instructions for reversal and UHS-Qualicare refused to comply, then UHS-Qualicare would have been considered to have breached "the covenant of good faith and fair dealing implied in law in all contracts in . . . [Mississippi]."[54] Thereafter

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[45] *Id.*

[46] *Id.* at 752. On this point the Mississippi Supreme Court noted "UHS-Qualicare's claim against Gulf Coast [Inc.] is correctly denominated a counterclaim. Rule 13(A), Miss. R. Civ. P. None of the other so-called counter-defendants . . . were original plaintiffs. UHS-Qualicare's claims against them are third party claims. Rule 14, Miss. R. Civ. P." *UHS-Qualicare*, 525 So. 2d at 758 n.10.

[47] *UHS - Qualicare*, 525 So. 2d at 752. The trial court stated:

> The Court cannot imagine anything more vital to a hospital than control of its rates. Here we have a substantial increase without consent of the hospital. The implementation of a new budget without Board approval was in aid of the rate raise. These two matters in the opinion of the court are substantial and material breaches and have not been cured.

Id.

[48] *Id.* at 753.

[49] *Id.*

[50] *Id.* at 757.

[51] *Id.* at 755-56. The Mississippi Supreme Court noted that it would reverse factual findings of a trial judge sitting without a jury only when such findings were "clearly erroneous" and findings of law whenever a trial judge findings are merely erroneous. *Id.* at 754. ("That the trial judge may have come close is not good enough.")

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[52] *UHS - Qualicare*, 525 So. 2d at 755-56. In reaching this declaration the court noted that it was "confronted . . . with a problem of private lawmaking . . . . [in the form of] the Management Agreement . . . ." and that "[p]ublic law merely furnishes tools whereby [the court] may assign meaning to the primary law made by the parties." *Id.* at 754. Thereafter the court stated:

> Today's case is a tailor-made reminder that the primary function of our law of contracts is "to deter people from behaving opportunistically toward their contracting parties." POSNER, ECONOMIC ANALYSIS OF LAW 81 (3d ed. 1986). Proceeding on the assumption that each party is a rationally self-interested wealth maximizer, our law allows parties such as these great freedom to strike their own deal. We imply into those contracts only such terms as may be expected to fill out the parties' agreement and reasonable expectations.

UHS-Qualicare, 525 So. 2d at 755.

Focusing on the "deal" of the parties, the court noted that the contract provided "no express directive" declaring it a material breach when one party "acts with respect to a matter where the other has unqualified authority . . ." *Id.* Looking to the content of the contract the court focused on the following language: "[i]f manager shall fail to keep, observe or perform any material covenant, agreement, term or provision of this agreement to be kept, observed or performed by a manager . . . ." then such failure shall lead to termination of the contract upon proper notice by Gulf Coast, Inc. *Id.* After noting that the placement of "material" in the contract language did not modify the words "fail to keep . . . [etc]" the court stated "[w]e think it established law . . . that a clause such as this should have implied into it the concept of material breach." *Id.* at 755-56. In addition the court held that if parties wish to exclude the concept of material breach "from their contract," they must do so clearly. *Id.*

[53] *Id.* at 756-57. On this point the court asserted that the "key to understanding why UHS-Qualicare's breach was not material lies in the total and absolute authority of Gulf Coast to undo that breach and its effect — and to do so immediately." *Id.* at 756.

[54] *Id.* at 757. Hereafter the court stated:

> Every contract contains an implied covenant of good faith and fair dealing. *See, e.g.*, Ohashi v. Verit Indus., 536 F.2d 849, 853 (9th Cir. 1976); Gulf Atl. Life Ins. Co. v. Barnes, 405 So. 2d 916, 924 (Ala. 1981); Corwin Chrysler-Plymouth v. Westchester Fire, 279 N.W.2d 638 (N.D. 1979); Christian v. American Home Assurance Co., 577 P.2d 899, 504 (Okla. 1977); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 306 (1979) ("Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforce-

the court, by reason of its action in the principal claim, held the judgment dismissing the UHS-Qualicare's counterclaim to be reversed and remanded for further proceedings.[55]

B. Damages

In 1987, the Mississippi Supreme Court was called on to review numerous damage awards in breach of contract cases. For the most part such review consisted of the application of routine contract principles. However, two cases, *South Central Bell v. Epps*[56] and *Lovett v. C.L. Garner, Inc.*[57] involved interesting and elucidating principles of contract law not at issue in most cases where money damages are sought for the breach of a contract.

In *Epps*, the court upheld a sizable damage award for mental anguish and physical pain and suffering as compensatory damages in an action for breach of a telephone service contract.[58] However, the *Epps* court ruled that the trial judge had erred in giving a punitive damage instruction to the jury where the telephone company's conduct was "more the product of oversight, inadvertence, or incompetence rather than the product of gross, callous or wanton conduct manifesting reckless indifference to the consequences of their act or the rights of the subscriber."[59]

In *Epps*, an elderly lady who lived alone in rural Mississippi received seemingly conflicting letters from South Central Bell directing her on how to avoid a disconnection of telephone service to her residence.[60] The letters were intended to be sent in a certain sequence but unfortunately were received by Mrs. Epps in reverse order.[61] The first letter Mrs. Epps received informed her that a deposit was due in order

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ment;") and POSNER, ECONOMIC ANALYSIS OF LAW 81 (3d Ed. 1986). *But see* Griffin v. Ware, 457 So. 2d 936, 940 (Miss. 1984).

UHS - Qualicare, 525 So. 2d at 757 n.8.

[55] *UHS-Qualicare*, 525 So. 2d at 758.

[56] 509 So. 2d 886 (Miss. 1987).

[57] 511 So. 2d 1346 (Miss. 1987).

[58] *Epps*, 509 So. 2d at 895. The jury awarded Mrs. Epps $75,000 in compensatory damages. *Id.* at 888.

[59] *Id.* at 893. Furthermore, the court stated that "[t]here is no evidence to indicate that Bell's employees acted maliciously or with some deliberate design to cause Mrs. Epps harm. Further we cannot say that Bell's misconduct constituted gross negligence so as to bring this case out of the ordinary rule and warrant submitting the issue of punitive damages to the jury." *Id.*

[60] *Id.* at 889.

[61] *Id.*

to continue the phone service to her residence.[62] Thereafter, Mrs. Epps arranged to pay the deposit in monthly installments.[63] However, Mrs. Epps subsequently received another letter, referred to by the phone company as "mailed warning deposit letter number 1," which informed her that if she paid her bills on or before the due date then no deposit would be necessary to continue her services.[64]

Thereafter Mrs. Epps paid her monthly bill, three days prior to its due date.[65] South Central Bell's computerized records reflected this payment,[66] but without any additional notice to Mrs. Epps, the phone company disconnected her phone service because she had failed to pay the agreed upon deposit installment.[67] Mrs. Epps' phone service was reconnected several days later, but only after she paid a deposit smaller than the previously requested deposit.[68] Shortly thereafter, Mrs. Epps was hospitalized for seven days and treated for a variety of illnesses, including chest pains, headaches, bronchitis, elevated blood pressure and blackouts.[69]

Subsequently, Mrs. Epps sought to recover compensatory and punitive damages from South Central Bell in an action alleging the latter "wrongfully terminated her telephone services causing her to suffer extreme mental anguish and other pain . . . ."[70] Mrs. Epps also alleged that South Central Bell's conduct was "willful, wanton, reckless, and intentional so as to demonstrate a disregard for her rights as a subscriber."[71] For its part South Central Bell argued that its agents had acted lawfully and in accordance with the general subscribers' services tariff in terminating Mrs. Epps' telephone service.[72] At trial, Mrs. Epps produced medical testimony that her hospitalization was necessitated by "an acute anxiety reaction, secondary to harassment from the telephone company" and that the deposit had been required because of her advanced age and health.[73] The trial judge submitted both the compensatory and punitive damage issues to the jury and the latter returned a verdict in favor of Epps, awarding her $75,000.00 in compensatory damages and $3,000,000.00 in punitive damages.[74]

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[62] *Id.* In April of 1982, Mrs. Epps received a letter, dated April 6, 1982, from South Central Bell. *Id.* This letter informed Mrs. Epps that the phone company would require her to deposit $515.00 by April 13, 1982 in order to continue service to her residence. *Id.*

[63] *Id.*

[64] *Id.* This letter was dated April 20, 1982. Both letters were sent by the same Bell employee and both letters were entered into Bell's computer system under Mrs. Epps' account. *Id.* The Bell employee who sent the letters testified at trial that "the two letters were sent out in the wrong sequence by mistake." *Id.*

[65] *Id.* Mrs. Epps made this payment on May 3, 1982. *Id.*

[66] *Id.* Payment was entered in Bell's system on May 6, 1982. *Id.*

[67] *Id.*

[68] *Id.* at 890. Reconnection occurred after Mrs. Epps' daughter and Don Barrett, a Mississippi attorney, interceded on behalf of Mrs. Epps and contacted Bell employee Pat Santucci. *Id.* Both Mrs. Epps' daughter and Barrett testified at trial that Santucci stated that deposit was required because of Mrs. Epps' advanced age and questionable health. *Id.* Santucci denied making such statements but did testify that she agreed to reduce the deposit and to immediately reconnect service to Mrs. Epps' residence upon payment of the deposit of $200.00. *Id.*

[69] *Id.* During the course of her hospital stay "Mrs. Epps developed a condition of involuntary voiding of her urine and continued to suffer from that condition after she was released from the hospital." *Id.*

[70] *Id.* at 888.

On appeal, the Mississippi Supreme Court concluded that the relationship between South Central Bell and its subscribers is governed by rules or tariffs promulgated by the phone company and submitted to and approved by the Mississippi Public Service Commission.[75] In addition, the court found the phone company breached the subscriber's tariff because the company had unequivocally waived the deposit requirement by the letter that notified Mrs. Epps that "the deposit would not be required provided she paid her bills on or before the due date."[76] Thus, nonpayment of the deposit was unavailable as a defense to wrongful termination of services.[77] As to the compensatory damage award, the court stated:

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[71] *Id. See infra* note 75 and accompanying text for discussion of the subscribers' tariff.

[72] *Epps*, 509 So. 2d at 888.

[73] *Id.* at 894-95.

[74] *Id.* at 888.

[75] *Id.* at 890-91. The court noted that "[t]raditionally, telephone companies have made rules and regulations for conducting their business. Such regulations necessarily include rules concerning payment for services, prepaid deposits as a prerequisite involving the termination of services where a subscriber fails to comply with company rules and regulations." *Id.* (citations omitted). In addition, the court concluded that "telephone companies retain exclusive control over the service they provide to the public" which gives the former "a superior position in their dealings with the public." *Id.* Given the unequal bargaining position of the parties to a phone service contract, the court recognized that the Mississippi legislature had created the Mississippi Public Service Commission [PSC] to "act on behalf of the public in regulating utilities" such as the telephone company. *Id.* Turning to the relationship of the PSC and South Central Bell the court stated:

> By statute, telephone companies still retain the right to make rules and regulations concerning the operation of their business. However, these rules, or tariffs, must be submitted and approved by the Public Service Commission before they are valid and binding on the subscribers. *See* MISS. CODE ANN. § 77-3-33(2) (1982).

Epps, 509 So. 2d at 891. Thereafter the court declared "we hold today that once such tariffs are approved by the [PSC], they are to be considered a part of the service contract between the telephone company and the subscriber." *Id.*

[76] *Id.* at 892. The court stated that initially the phone company was justified in

> As a general rule, the measure of compensatory damages for breach of a telephone service contract is the amount which will compensate the injured subscriber for all losses and damages sustained as a direct or approximate consequence of the breach of that contract. Additionally, we have held that where telephone services are wrongfully disconnected, the subscriber is entitled to recover actual damages as well as damages occasioned by the inconvenience and the annoyance caused by the deprivation of services. However, damages for physical pain and suffering or mental pain and suffering are generally not recoverable absent a showing that the telephone company had knowledge of some special circumstances surrounding the subscriber's account which could cause such damages to occur. (citations omitted).[78]

Upon reviewing the trial record, the Mississippi Supreme Court concluded that South Central Bell knew of Mrs. Epps' special circumstances and that wrongful termination of her services "could cause her to suffer both mental anguish and physical pain and suffering . . . ."[79]

In *Lovett v. E. L. Garner*,[80] the court reviewed a damage award in an action for breach of a gasoline retailing agreement.[81] At trial, the nonbreaching party was allowed to recover profits lost because of the

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requiring Mrs. Epps to post a deposit since the tariff authorized the company to require deposits from certain risky customers, of which Mrs. Epps was one, based on her long distance charges consistently exceeding her toll credit limit. *Id.* However, the court concluded that the power which South Central Bell retained over creating and enforcing rules concerning their business practices also allowed them "to waive such rules, at their option, either expressly or by implication." *Id.*

[77] *Id.* Thereafter the court held that "[t]here can be no question that the April 20 letter constituted a waiver of the deposit . . . . Once such a regulation or rule is waived, non-compliance by a subscriber will not serve as a defense to a claim of wrongful disconnection by that subscriber." *Id.* In addition, the court noted that the defense of equitable estoppel might be available to Mrs. Epps since the court could not "say . . . [she] unreasonably relied on the April 20th letter." *Id.*

[78] *Epps*, 509 So. 2d at 894. The court concluded that "[t]here can be no question that she also suffered extreme mental anguish due to the incident, which undoubtedly aggravated her previous health problems. These injuries, both mental and physical, were a direct and proximate result of the breach of the subscribers' contract." *Id.* at 895.

[79] *Id.*

[80] 511 So. 2d 1346 (Miss. 1987).

[81] *Id.* at 1347.

breach of the contract.[82] On appeal, the court stated:

> In Mississippi, one may recover for loss of future profits in a breach of contract action so long as such profits are proved with reasonable certainty, not based on speculation or conjecture. . . . In calculating loss of future profits, such loss is that of net profits as opposed to gross profits. . . . To ascertain net profits, a party must deduct such items as overhead, depreciation, taxes and inflation. Further, future profits should always be discounted at an appropriate rate to arrive at present value. And, finally, the plaintiff must mitigate damages if he is able to do so. (citations omitted)[83]

Thereafter, the *Lovett* court concluded that the nonbreaching party's evidence was "legally insufficient to undergird a damage award . . . for loss of future profits . . . ."[84] This finding of insufficiency was based on the court's conclusion that the nonbreaching party's evidence of past profits was misleading[85] and the general calculation of future profits ignored "[v]ariables such as inflation, market availability, etc. . . . . [with the] future profits arrived at . . . not discounted to present value . . . ."[86]

II. Uniform Commercial Code

A. *Retention of Collateral by Secured Party*

In the 1987 case of *Millican v. Turner*,[87] the Mississippi Supreme Court considered "under what circumstances may a creditor who has repossessed collateral be deemed to have retained that collateral in satisfaction of the debt which it secures."[88] In reaching this decision the court noted that this was a question of first impression for Mississippi and that its answer turned on what interpretation the court would give section 75-9-505(2) of the Mississippi Code.[89]

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[82] *Id.* at 1349. Garner, the non-breaching party, computed loss of future profits by taking one-half (½) of the net profits for a nine month period during which the contract was complied with, adding the sums for each of these months, to arrive at a total and then dividing this total by the number of months to obtain a monthly average. This average was then multiplied by the fifty-one months remaining on the contract at the time of the breach to arrive at a total of $38,615.16. The chancellor adopted this figure when making his damage award. *Id.* at 1352.

[83] *Id.* at 1353.

[84] *Id.*

[85] *Id.* The contract guaranteed Lovett, the breaching party, a four-cent per gallon profit which was to be deduced prior to any payment of the contractual agreement upon one-half (½) net profits to Garner.

[86] *Id.*

[87] 503 So. 2d 289 (Miss. 1987).

[88] *Millican*, 503 So. 2d at 291. The trial court had also held that Millican's retention

Section 75-9-505(2) provides that a secured party in possession of collateral may, after default of the debt which such collateral secured, propose to retain the collateral in satisfaction of the obligation in any case involving either nonconsumer goods[90] as collateral or consumer goods as collateral where the debtor has paid less than sixty percent (60%) of the cash price of such goods and in which the secured party has a purchase money security interest or where the debtor has paid less than sixty percent (60%) of a loan in the case of any other secured interest in consumer goods.[91] If, after giving notice of such a retention proposal to the debtor and in certain cases, other secured parties,[92] the secured party in possession of the collateral receives no written objection to her proposal then the latter may retain the collateral in satisfaction of the debtor's obligation.[93]

In *Millican*, the purchaser of an automobile entered into a retail installment contract with the seller of the vehicle.[94] On the day of the sale, the seller assigned his rights under the contract to a local bank.[95] As part of the assignment, the seller agreed to repurchase the contract

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of the property for more than two (2) years constituted a common law accord and satisfaction. *Id.* at 290. On appeal, Turner's counsel conceded that the repossession did not constitute accord and satisfaction. *Id.* at 291. *See generally* Sherman-Williams v. Sarrett, 415 So. 2d 1332, 1334 (Miss. 1982) (listing elements of accord and satisfaction).

[89] *Millican*, 503 So. 2d at 291. The court quoted § 75-9-505(2), which reads as follows:

> In any other case involving consumer goods or any other collateral, a secured party in possession may, after default, propose to retain the collateral in satisfaction of the obligation.
>
> Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subsection.

Millican, 503 So. 2d at 291.

[90] The Uniform Commercial Code, as adopted by Mississippi, provides: "Goods are (1) 'consumer goods' if they are used or bought for use primarily for personal, family or household purposes . . . ." MISS. CODE ANN. § 75-9-109(1) (1972).

[91] MISS. CODE ANN. § 75-9-505(2) (1972).

[92] Except in cases involving consumer goods written notice of a proposal to retain collateral must be sent to "any other secured party who has a security interest in the collateral and who has duly filed a financing statement indexed in the name of the debtor in this state or is known by the secured party in possession to have a security interest in it." MISS. CODE ANN. § 75-9-505(2) (1972).

[93] *Id.*

[94] *Millican*, 503 So. 2d at 290. The contract was entered into on May 28, 1979. *Id.*

[95] *Id.*

from the assignee upon the latter's demand.[96] Subsequently, the buyer ceased making the payments required by the contract and the bank repossessed the automobile.[97] The bank also exercised its right to reassign the contract to the seller.[98] The seller repurchased the contract from the bank and paid the latter the outstanding amount owed on the contract.[99] The automobile remained on the premises of a car dealer who had repossessed the car for the bank but the car was placed at the seller's disposal.[100] The seller was unsuccessful in his attempts to resell the automobile and abandoned these effort some twelve months after the reassignment.[101]

Six months after the reassignment the seller filed suit against the buyer alleging breach of contract and prayed for the sums he paid the bank, plus interest, collection fee and costs.[102] In her answer the buyer asserted, as an affirmative defense, that the seller had elected to retain the automobile in satisfaction of the debt.[103] The trial court found that the seller's retention of the property for some two years constituted a retention of collateral in satisfaction of the obligation and granted summary judgment on this issue.[104]

On appeal, the Mississippi Supreme Court recognized that several other state courts had construed their counterparts of section 75-9-505(2), and three distinct views had developed as to what constituted the retention of collateral in satisfaction of a secured debt.[105] The court rejected one view which held a creditor would be deemed to have retained the collateral in satisfaction of the debt only after the creditor had given notice to the debtor of his intentions to do so.[106] The court also rejected the view that a creditor must have manifested an intent to retain the collateral before he can be deemed to have accepted it in satisfaction of a debt.[107]

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[96] *Id.*

[97] *Id.* The opinion recites:

> After several months, Turner stopped making payments, and [the bank] employed Bob Shirley, a car dealer, to repossess the Buick. Turner claimed the repossession took place in August or December of 1979; Millican claimed it occurred in the spring of 1981. When Shirley found the car . . . [it appeared] as if it had been abandoned. Shirley took the car to his place of business, where it remained until and throughout the litigation which is the subject of this appeal.

Id.

[98] *Id.*

[99] *Id.* The reassignment occurred in July of 1981. *Id.*

[100] *Id.*

[101] *Id.*

[102] *Id.*

[103] *Id.*

[104] *Id.*

[105] *Id.* at 291.

[106] *Id. See* Flickinger v. Genesee Corp., 423 N.Y.S.2d 73, 76 (1979) (cited in

Instead, the court adopted a third view, also the majority view, holding that a creditor who has repossessed collateral and retained it for an unreasonable period of time without disposing of it is deemed to have retained the collateral in satisfaction of the debt which the collateral secured.[108] Furthermore, the court held that what constituted unreasonable delay should be decided by the trier of fact.[109] Such factors as the type of collateral, the speed of its depreciation, the market for such collateral and other relevant circumstances were recognized by the court as being important to a determination of reasonableness of delay.[110] The court also noted that often expert testimony would be helpful to the trier of fact and suggested that in the present case used car dealers might aid the trier of fact in determining the reasonableness of the seller's actions or inactions.[111] Since the question of unreasonable delay had not been submitted to the jury, the court remanded the case for a trial on the merits.[112]

B. *Implied Warranty of Merchantability and Used Goods*

In *Beck Enterprises, Inc. v. Hester*,[113] a case ultimately decided under a theory of fraud, the Mississippi Supreme Court discussed in detail the use of the implied warranty of merchantability by the purchasers of used goods where those goods fail to conform to the quality of other similar used goods.[114]

Beck involved the purchase of a used pick-up truck by a husband

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Schmode's Inc. v. Wilkinson, 361 N.W.2d 557, 558 (Neb. 1985)).

[107] *Id. See* Nelson v. Armstrong, 582 P.2d 1100 (1978)(undue delay in disposing of collateral insufficient to manifest intent to retain it).

[108] *Millican*, 503 So. 2d at 291. The court stated that this position, "appears to be the majority position and cited the following cases as support: Swanson v. May, 697 P.2d 1013 (Wash. 1985); Wisconics Eng'g, Inc. v. Fisher, 466 N.E.2d 745 (Ind. Ct. App. 1984); Service Chevrolet, Inc. v. Sparks, 660 P.2d 760 (Wash. 1983); Farmer's State Bank v. Ballew, 626 P.2d 337 (Okla. Ct. App. 1981); Shultz v. Delaware Trust Co., 360 A.2d 576 (Del. Super. Ct. 1976); Moran v. Holman, 514 P.2d 817 (Alaska 1973). *Millican*, 503 So. 2d at 291 n.2.

[109] 503 So. 2d at 291 (citations omitted).

[110] *Id.*

[111] *Id.*

[112] *Id.* at 292.

[113] 512 So. 2d 672 (Miss. 1987).

[114] *Id.* at 675-76.

and wife.[115] This purchase was financed by an entity which was separate but not unrelated to the seller.[116] Almost immediately the couple began experiencing mechanical trouble with the truck[117] and after six months of ownership the couple brought suit seeking compensatory damages, punitive damages, rescission of the contract of sale and rescission of the financing contract.[118] The trial court allowed the case to go to the jury on both the fraud and breach of warranty theories.[119] The jury returned a general verdict in favor of the purchasers, awarding them actual damages of $3,433.00 and punitive damages of $750.00[120]

On appeal, the Mississippi Supreme Court noted that the case was filed prior to the date Mississippi's Motor Vehicle Warranty Enforcement Act became effective.[121] Thereafter the court stated that the case was "grounded in the Uniform Commercial Code as well as non-code common law principles."[122] Focusing on the theory that the seller of the truck breached the implied warranty of merchantability, the court cited section 75-2-314 of the Mississippi Code which reads:

> (1) A warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind . . . .
>
> (2) Goods to be merchantable must be at least such as . . . (c) are fit for the ordinary purposes for which such goods are used.[123]

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[115] *Id.* at 674.

[116] *Id.* The Hesters financed part of the purchase price with Coast Financial Services, Inc., of which Johnny Beck was president. *Id.*

[117] *Id.*

[118] *Id.*

[119] *Id.*

[120] *Id.*

[121] *Id.* at 674 n.1. The Motor Vehicle Warranty Enforcement Act is codified at MISS. CODE ANN. § 63-17-151 to 165 (Supp. 1986).

[122] *Beck Enters.*, 512 So. 2d at 674. Thereafter the court stated "The Court notes that among the general principles stated in the Code is MISS. CODE ANN. § 75-1-103 (1972) providing that common-law principles of fraud and misrepresentation supplement the Code provisions as follows:

> Unless displaced by the particular provisions of this Code, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principle and agent, estoppel, *fraud, misrepresentation*, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplements its provisions. (emphasis added).

MISS. CODE ANN. § 75-1-103 (1972).

[123] 512 So. 2d at 675.

Since "[n]o question was raised regarding the seller's status as a 'merchant with respect to' the sale of a truck," the court focused on the question of "the applicability of implied warranties to the sale of used motor vehicles."[124] The court concluded that "the UCC does not distinguish between new and used 'goods'[125] and that the implied warranty of merchantability applies to the sale of used motor vehicles by a 'merchant with respect to goods of that kind'."[126] Thereafter the court stated:

> Merchantability is different for new and used goods of the same type. Used goods are reasonably expected to require more maintenance and repair, . . . [U]sed goods should be compared to similar used goods. If they conform to the quality of other similar used goods, they will normally be merchantable.[127]

As for the steps a buyer must take after such a breach of warranty has occurred, the court stated that "[w]hen a buyer has accepted goods[128] and subsequently discovers a breach of the implied warranty of merchantability, the buyer may invoke section 75-2-608 Miss. Code Ann. (1972) . . . ."[129] This section provides that where a buyer accepts a "commercial unit"[130] which has a nonconformity which substantially impairs the value of the unit and this nonconformity was not discoverable by the buyer, or the buyer accepted on the reasonable assumption that the nonconformity would be cured,[131] then the "buyer may revoke acceptance of the goods within a reasonable time after the nonconformity was discovered or should have been discovered . . . ."[132] In *Beck*, the court found that the buyers had not met the requirements of section 75-2-608[133] but held that "there was sufficient evidence on disputed testimony to present a jury question on the issue of common law fraud"[134] and it was upon this latter issue that the court ultimately rested its decision to uphold the jury award of compensatory damages.[135]

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[124] *Id.*

[125] *Id.* at 676. MISS. CODE ANN. § 25-2-105 (1972) defines goods as "all things . . . which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities . . . and things in action."

[126] *Beck Enters.*, 512 So. 2d at 676. The court stated "The implied warranty of merchantability is not intended to guarantee that the goods be the best or of the highest quality - the standard is measured by the generally acceptable quality under the description used in the contract." *Id.* (citing Dickerson v. Mountain View Equipment Co., 710 P.2d 621, 624 (Idaho 1985)).

[127] *Beck Enters.* 512 So. 2d at 676.

[128] Acceptance of goods by a buyer is defined in MISS. CODE ANN. § 75-2-606 (1972).

[129] *Beck Enters.*, 512 So. 2d at 676.

[130] A commercial unit "means such a unit of goods as by commercial usage is a single whole for purposes of sale . . . .". MISS. CODE ANN. § 75-2-105(6) (1972).

[131] If the defect is not discovered before or contemporaneously with acceptance, a buyer of goods may revoke acceptance if such nondiscovery was reasonably induced by the difficulty of the discovery or by assurances from the seller. *Beck Enters.*, 512 So. 2d at 676 (citing Rester v. Morrow, 491 So. 2d 204, 210 (Miss. 1986) and WHITE AND SUMMERS, UNIFORM COMMERCIAL CODE § 8-3, p. 303 (2d ed. 1980)).

In *Hargett v. Midas International Corp.*,[136] the Mississippi Supreme Court once again applied the implied warranty of merchantability to used goods.[137] In this case the used good was a motor home.[138] Soon after purchasing the motor home from a car dealership,[139] the buyer "allegedly endured a series of difficulties with the motor home to the extent that [the buyer] describe[d] the motor home as having 'completely fallen apart'."[140] The buyer attempted to have the motor home repaired but when such repairs were not made to his satisfaction, he filed suit against the manufacturer of the motor home alleging negligence and breach of the implied warranty of merchantability.[141] The manufacturer filed a motion for summary judgment, contending it was not a seller within the meaning of section 75-2-103 of the Mississippi Code and therefore not liable for any breach of the implied warranty.[142] The trial court granted the manufacturer summary judgment on the issues of negligence and breach of the implied warranty and the buyer appealed.[143]

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[132] *Beck Enters.*, 512 So. 2d at 676. Continuing, the court stated that "[o]nce acceptance has been properly revoked, the buyer may cancel the contract and recover so much of the price as has been paid. MISS. CODE ANN. § 75-2-711(1) (1972)." *Beck Enter.*, 512 So. 2d at 676. Proper forms notice of revocation are found at MISS. CODE ANN. § 75-2-608 (1972). The court also noted that "[r]evocation of acceptance and recovery of payments made is distinguished by White and Summers . . . at p. 375 from accepting non-conforming goods and suing for damages under MISS. CODE ANN. § 75-2-719 (1972)." *Beck Enters.*, 512 So. 2d at 676 n.5.

[133] 512 So. 2d at 677.

[134] *Id.*

[135] *Id.* at 678.

[136] 508 So. 2d 663 (Miss. 1987).

[137] *Hargett*, 508 So. 2d at 664.

[138] *Id.* at 663.

[139] The used motor home was purchased from Windham Ford Company on April 9, 1979. *Id.* The motor home was manufactured by Midas International, a foreign corporation. *Id.* at 663-64.

[140] *Id.* at 664.

[141] *Id.*

[142] *Id.*

[143] *Id.*

Initially, the Supreme Court of Mississippi repeated its ruling that used goods are subject to the implied warranty of merchantability.[144] Next, the court held that since the manufacturer "sells or contracts to sell motor homes" to anyone, not necessarily the buyer who seeks to invoke the implied warranty, then the manufacturer is "a seller as defined by section 75-2-103(1)(d)."[145] Thereafter the court stated that the "issue becomes whether [the manufacturer] was 'the seller' as contemplated by section 75-2-314" since the buyer was not in privity with the manufacturer."[146] Relying on section 11-7-20 of the Mississippi Code, which provides that privity shall not be a requirement to maintain actions brought under the Uniform Commercial Code, the court held that the buyer could maintain an action for breach of the implied warranty against the manufacturer as a seller even though no privity existed between the two.[147] In addition, the court stated that "[t]o recover, [the buyer] must not only prove the motor home was unmerchantable as defined by section 25-2-314 of the Mississippi Code, but also establish the defects existed when the motor home left the [manufacturer's] control."[148] Such a requirement, the court reasoned, would not impose a greater burden on manufacturers, but simply require them to produce merchantable goods.[149]

III. BANKS AND BANKING

A. *Rights to Set-off*

The court decided two cases, *Central Bank of Mississippi v. Butler*[150] and *Deposit Guaranty National Bank v. B.N. Simrall & Sons, Inc.*[151] in which the payees of dishonored checks sought to recover money damages from payor banks[152] which refused to honor these checks.[153]

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[144] *Id.* The court stated:

> Because the [UCC] does not distinguish between new and used goods, the implied warranty of merchantability applies to the sale of both new and used goods so long as "the seller is a merchant with respect to goods of that kind. "If a product conforms to the quality of other similar products in the market, it will normally be merchantable." *Hargett*, 508 So. 2d at 664. (citations omitted).

[145] *Id. at 665.*

[146] *Id.* The court noted that the buyer did not purchase the used goods directly from the manufacturer or from someone acting as the agent of the manufacturer and that the manufacturer made no express warranties at the time the motor home was sold by Windham Ford Company. *Id.*

[147] *Hargett*, 508 So. 2d at 665.

[148] *Id.*

[149] *Id.*

[150] 517 So. 2d 507 (Miss. 1987).

[151] 524 So. 2d 295 (Miss. 1987).

In each of these cases the checks were dishonored because the funds in the accounts were insufficient to cover the amount of the drafts.[154] Equally similar in both cases was the fact that the deficiency in the accounts was brought about by the banks who withdrew funds from the accounts to satisfy debts owed the banks.

The case of *B.N. Simrall & Sons* construed the general rule that before a third party can claim "ownership of certain funds, he must make a showing of the special character of the deposit, whether by trust fund, special deposit or fiduciary relationship."[155] *Simrall* involved a complex factual situation, but it suffices to state that one member of a joint venture made a wire transfer to the other member's general business account to cover checks drawn on this account and issued to third parties, including B.N. Simrall & Sons, Inc., who were doing business with the joint venture.[156] The bank received the wire transfer and credited the account.[157] Meanwhile, the general account was used for a number of transfers, receiving deposits from various sources and paying out funds to an equally diverse number of payees.[158] Prior to the presentment for payment of checks issued to the third parties doing business with the joint venture, the bank seized the funds in the general account, including the funds received by the wire transfer which were to cover these checks, and applied the funds to the debts owed the bank by the holder of the account.[159] When Simrall's check was presented for payment, it was dishonored and returned to the collecting bank marked "insufficient funds."[160] Collection of the funds from the drawer of the check being doubtful, Simrall brought suit against the bank.[161] The trial judge found that neither a trust fund nor a special deposit had been established by the evidence presented, but allowed the case to go to the jury under a theory of constructive trust or conversion.[162] The jury returned a judgment in favor of Simrall.[163]

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[152] A payor bank "means a bank by which an item is payable as drawn or accepted." MISS. CODE ANN. § 75-4-105(b)(1972). *See also* MISS. CODE ANN. § 75-3-507 (1972)(defines when instrument is dishonored).

[153] *Central Bank*, 517 So. 2d at 508-09; *B.N. Simrall & Sons*, 524 So. 2d at 298-99.

[154] In *Central Bank*, the bank used the funds in an account maintained by one business to offset a debt owed by a separate business with the sole connection between the two businesses being that they shared the same primary stockholder. *See infra* notes 170-77 and accompanying text. In *B.N. Simrall & Sons*, the account and debt involved in the setoff were maintained and owed by the same entity. *See infra* notes 156-60 and accompanying text.

[155] *B.N. Simrall & Sons*, 524 So. 2d at 300.

[156] *Id.* at 296-98.

[157] *Id.* at 298.

[158] *Id.*

[159] *Id.*

[160] *Id.*

On appeal, the Mississippi Supreme Court found that the bank had the authority to seize the deposit and apply it against the account holder's indebtedness and reversed and rendered a decision in favor of the bank.[164] The court stated that it was a well-settled rule that funds deposited in a general account belong to the bank as debtor of the one in whose name the account exists.[165] The court also noted that it was an equally well-settled rule that a bank, under the "set-off principle", has the right to apply a debtor's deposit to the payment of his debt then due and that such right exists completely independent of any security agreement specifically authorizing a bank to take such action.[166] Having summarized the relationship between a bank and its depositors/debtors and finding the account in question to be a general account, along with the lack of any knowledge on the part of the bank as to any special limitations on the deposit, the court held that "the giving of a check by a depositor does not constitute an assignment of the funds on deposit. The bank may refuse to pay the check . . . and the holder of the check has no cause of action against the bank"[167] absent

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[161] *Id.* at 299.

[162] *Id.*

[163] *Id.*

[164] *Id.* at 301-02.

[165] *Id.* at 300. (citing Deposit Guar. Bank & Trust Co. v. Merchants Bank & Trust Co., 171 Miss. 553, 158 So. 136 (1934)).

[166] *B.N. Simrall & Sons*, 524 So. 2d at 300. In commenting on the set-off principle, the court stated:

> It has been stated that it would be inequitable to permit a depositor to carry an open account in the bank which would induce the bank to feel secure in granting a certain line of credit, and then permit the debtor to apply the funds to another purpose than satisfying the debt simply because the debtor-depositor had not expressly agreed to apply the deposit to the debt due the bank.

Id. The court added that a bank's right of set-off exists even if a bank's indebtedness is secured by collateral pursuant to a security agreement. *B.N. Simrall & Sons*, 524 So. 2d at 300 (citing Duncan v. Coahoma Bank, 397 So. 2d 891, 893 (Miss. 1981)).

[167] 524 So. 2d at 300 (citing Citizens Nat'l Bank v. First Nat'l Bank, 347 So. 2d 964, 968 (Miss. 1977). The court stated:

> It is now, and has been for a long time, the law in this State, that the relationship between a bank and its depositors is one of debtor and creditor. Since it is a debtor-creditor relationship, the giving of a check by a depositor does not constitute an assignment of the funds on deposit. The bank may refuse to pay

"a showing of the special character of a deposit, whether by trust funds, special deposit or fiduciary relationship."[168]

Having established the general rule that a bank may seize deposits to satisfy the debts of a depositor/debtor without fear of recourse by innocent third parties who hold checks drawn on the depositor/debtor's account, the court also had occasion to apply the trust account exception to that rule and held a bank liable for checks dishonored following depletion of an account by set-off.[169] This occasion was presented in *Central Bank of Mississippi v. Butler*, wherein a livestock auction house, pursuant to federal regulations,[170] maintained a custodial account with a bank out of which the sellers of livestock were to be paid.[171] The auction house also maintained a general account with the same bank.[172] It was the bank's practice to hold the checks of livestock buyers in this general account until the payor bank of these checks paid over the called for funds.[173] Thereafter the bank would transfer the funds to the custodial account and pay checks presented by livestock sellers.[174]

The primary stockholder of the auction house was also the primary stockholder of a totally separate business entity which maintained a general account with the same bank.[175] Subsequently, this separate entity's account became overdrawn and the Bank, without the authority of the primary stockholder, credited sums out of the auction house's general account to the other entity's overdrawn account.[176] This placed the auction house's accounts in an overdraft situation and when the livestock sellers presented their checks for payment the

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> the check, although the depositor has sufficient funds to his credit . . . and the holder of the check has no cause of action against the bank. The holder of the check must look to the drawer . . . and only the drawer of the check can complain about the bank not honoring the check.

B.N. Simrall & Sons, 524 So. 2d at 300.

[168] 524 So. 2d at 300.

[169] *See infra* notes 171-181 and accompanying text.

[170] The federal regulation involved is codified at 9 C.F.R. § 201.42 (1987) and provides that persons and organizations governed by the Packers and Stockyards Act, 7 U.S.C. §§ 181-229 (1980) must maintain a custodial account into which are to be deposited payments for livestock and such payments are described by the federal regulations as "trust funds." *Central Bank*, 517 So. 2d at 508.

[171] *Central Bank*, 517 So. 2d at 508.

[172] *Id.*

[173] *Id.*

[174] *Id.*

[175] *Id.*

[176] *Id.* at 509.

checks were dishonored.[177] The sellers thereafter prevailed in a suit brought against the bank in the Chancery Court of Rankin County.[178]

After noting the general rule, the Mississippi Supreme Court adopted the majority rule exception which posits that holders of checks may directly sue a bank where the deposits in question were "special," with title to the funds remaining in the depositor, thereby creating no debtor-creditor relationship between the bank and the depositor as with "general" deposits.[179] Thereafter the court upheld the trial court's award of actual damages and noted that when a bank has knowledge of a trust, special deposits or other types of fiduciary relationships between a depositor and a holder of a check drawn on the depositors account, then the bank cannot set-off such funds against the individual indebtedness of the depositor.[180]

B. *Usurious Loans*

During its 1987 term, the Mississippi Supreme Court rejected the claims of borrowers who sought to raise usury as a defense[181] or as the basis for recovery of amounts paid to a lender.[182] In the case of *Galloway v. Travelers Insurance Co.*,[183] an insurance company entered into an agreement with two business partners under which the partners would receive a fifteen million dollar loan.[184] A condition precedent to closing the loan was that the businessmen form a corporation which would be liable for the loan.[185] The businessmen were also required by the insurance company to transfer ownership of approximately 16,000 acres of real estate to the newly formed corporation as collateral to secure the loan.[186] The interest rate on the loan was 11.7819%, a rate which would be usurious if charged to an individual, but not usurious if charged to a corporation.[187] In due course the corporation was created and the loan was made to the corporation.[188] Neither of the two businessmen were personally liable on the note.[189] The corporation never transacted any business other than the loan.[190] One of the businessmen made all the payments on the note and the proceeds of the loan were used to retire debt previously incurred by the businessman and retire existing mortgages on parcels of the collateral acreage.[191] Of the fifteen million dollars, approximately two million dollars went directly to the newly formed corporation.[192] Ultimately, the corporation experienced financial trouble and conveyed to one of the businessmen the entire 16,000 acre tract, for which the businessman paid no consideration.[193] Following an unsuccessful attempt to sell the land to a third party, the businessman was forced to convey the land to the insurance company in lieu of foreclosure.[194] Subsequently the businessmen and the corporation brought suit against the insurance company, claiming that the corporation was formed solely to circumvent Mississippi's usury statute and seeking damages for tortious interference with business.[195]

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[177] *Id.*

[178] *Id.*

[179] *Id.* at 510-511.

[180] *Id.*

[181] *See supra* note 4.

[182] *See infra* notes 184-205 and accompanying text.

[183] 515 So. 2d 678 (Miss. 1987).

[184] *Galloway*, 515 So. 2d at 679.

[185] *Id.*

[186] *Id.*

[187] *Id.*

[188] *Id.*

On appeal of the trial court's decision to grant the insurance company's motion for summary judgment on both counts, the Mississippi Supreme Court declared the "instant appeal [to be] a case of first impression in our state with regard to the issue . . . [of] when an individual has formed a shell corporation solely for the purpose of obtaining a loan which would otherwise be usurious, and when the individual has used the proceeds of the loan for a business purpose, is the loan usurious?"[196] The court surmised that "[a]pparently the sole purpose of the incorporation was to make applicable the corporate, rather than the individual, ceiling on interest."[197] This single apparancy, according to the court, was not enough to give rise to a claim of usury.[198] In reaching this conclusion the court stated:

> [t]he corporate form offers various options to those who choose it. Among these options is the opportunity to pursue financing which is unavailable to those who have not incorporated. When

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[189] *Id.*

[190] *Id.*

[191] *Id.*

[192] *Id.*

[193] *Id.*

[194] *Id.* at 679-80.

[195] *Id.* at 680.

[196] *Id.*

[197] *Id.* The applicable usury statute was MISS. CODE ANN. § 75-17-1 (Supp. 1979). This code section has since been amended. *Galloway*, 515 So. 2d at 680 n.3.

[198] *Galloway*, 515 So. 2d at 681.

> an individual acting in furtherance of a profit-oriented business venture chooses to incorporate solely for the purpose of obtaining such financing, he will not later be heard to complain that the loan was usurious.[199]

The court added that a claim or defense of usury is "available when the proceeds of the loan are used to meet the individual's personal, non-business needs and obligations."[200] Therefore, the court found that no genuine issue of material fact existed at trial as to the loan having been used for business purposes and that summary judgment was properly granted the insurance company by the trial judge.[201]

Justice Reuben Anderson, joined by Justices Dan Lee and Sullivan, issued a strong dissent to the majority opinion.[202] Justice Anderson not only declared the majority opinion "a road map around [Mississippi's] usury statute" but also took the majority to task over the proper bounds of judicial lawmaking.[203] The following excerpt merely summarizes the dissent:

> Today's decision goes far beyond the "interstitial" legislation permitted to judges. Today we have repudiated a public policy dating from the time of the Mississippi territory. We have ignored a hundred years of our own case law. We have disregarded the clear intent of a statute and provided its would-be evaders with helpful instructions, because the statute evinces economic assumptions we consider outdated and unwise. In so doing, we have arrogated to ourselves the power to decide which of conflicting economic theories shall be the state's accredited doctrine.
>
> . . . we have assume the position of Mayor of the Palace, and relegated the legislature to the role of a Merovingian emperor.[204]

IV. ULTRA VIRES AND SUSPENDED CORPORATIONS

In 1983, Cook Construction Company entered into a subcontract with Bryant Construction Company under which the latter was to perform certain portions of highway construction work which the former was required to perform under a primary contract with the state.[205] In January 1984, the chairman of the Mississippi State Tax Commission, pursuant to section 27-13-27 of the Mississippi Code, suspended Bryant from performing any rights acquired by the corporate form of organization because Bryant had failed to file annual reports and pay franchise taxes.[206] While suspended, Bryant entered into a second and completely separate contract with Cook under which Bryant was to install castings and grates needed for the highway construction project.[207] This second contract was evidenced only by a memorandum on Cook Construction letterhead and signed by Cook personnel.[208] The memorandum purported to quote payment for labor on a per pound of casting or grates basis.[209] Bryant arguably performed the work called for by this second contract and sought payment from Cook according to the memorandum's terms.[210] Cook refused to pay and Bryant filed an action for a breach of contract against Cook in the circuit court, alleging breach of contract. Upon Cook's motion, the trial court dismissed the complaint finding that since Bryant was under suspension, it lacked both the power to contract and the power to sue.[211] Thereafter, Bryant's two shareholders successfully intervened in the action and together with Bryant filed an amended complaint.[212]

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[199] *Id.* The court aligned itself with those jurisdictions adhering to the "New York Rule" which holds that in such cases the usury law is not being evaded but followed to accomplish a result desired by the contracting parties. *Id.*

[200] *Id.*

[201] *Id.* at 682.

[202] *Id.* at 687.

[203] *Id.* at 689.

[204] *Id.* at 691-92.

Prior to the dismissal of Bryant's original complaint and the filing of the amended complaint, the State Tax Commission, which never sought to dissolve the suspended corporation, set aside Bryant's suspension.[213] However, the trial court dismissed the complaint a second time, finding the shareholders' claim to be derivative of the corporation's claim. By implication this dismissal was a denial of Bryant's motion for summary judgment which was also pending before the trial court.[214]

On appeal of the case styled *Bryant Construction Co., Inc. v. Cook*

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[205] Bryant Const. Co. v. Cook Const. Co., 518 So. 2d 625, 626 (Miss. 1987).

[206] *Id.* at 627.

[207] *Id.*

[208] *Id.*

[209] *Id.*

[210] *Id.*

[211] *Id.*

[212] *Id.*

[213] *Id.*

[214] *Id.*

Construction Co.,[215] the Mississippi Supreme Court reversed the trial court and remanded the case for a trial on the merits.[216] First, the court recognized that this appeal involved two distinct corporate incapacities: the inability to contract and the inability to sue.[217] With this distinction in mind, the court proceeded to construe section 27-13-27 of the Mississippi Code which provides that if a corporation fails to pay taxes called for by chapter 27, then the commissioner may suspend the right of that corporation to function as a corporation.[218] However, following the setting aside of such suspension, the corporation is "restored to all rights of which it was deprived by such suspension, and authorized to resume all activities as though said suspension had not been imposed."[219] The court stated that although a corporation may be suspended for failure to pay its franchise tax, unless the corporation is dissolved by affirmative action on the part of the state it is merely unable to operate and it does not cease to exist.[220]

Thereafter the court concluded that any action taken by a suspended corporation during the time of suspension is beyond the powers of the corporation or *ultra vires*.[221] Therefore, *ultra vires* was really the defense Cook had raised to the bringing of the lawsuit and the disputed contract.[222] So far as the contract was concerned, the court reiterated that one who accepts the benefits of a corporation's *ultra vires* agreement cannot later repudiate the agreement on those grounds.[223]

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[215] 518 So. 2d 625 (Miss. 1987).

[216] *Id.* at 631-32.

[217] *Id.* at 628.

[218] *Id.* at 629.

[219] *Id.* at 628.

[220] *Id.* at 629. Having never interpreted § 27-13-27 on prior occasions, the Mississippi Supreme Court considered an earlier decision in which it analyzed an almost identical statute. Carolina Transformer Co. v. Anderson, 341 So. 2d 1327, 1329 (Miss. 1977) (interpreting an almost identical statute found at MISS. CODE ANN. § 79-3-189 and holding that although suspended corporation became "functionally viable to operate, it did not cease to exist). The court also considered two "Erie guesses" made by the Fifth Circuit: Chevron Oil Co. v. Clark, 432 F.2d 280, 285 (5th Cir. 1970) (holding that dissolution of suspended corporation under § 27-13-27 required additional affirmative action by state); PLM v. E. Randle Co., 797 F.2d 204, 206 (5th Cir. 1986) (holding that power to sue is restored to corporation suspended under § 27-13-27 but that restoration is not retroactive so that any lawsuit must be filed after lifting of suspension) and concluded:

> When a corporation fails to pay its franchise tax . . . then the chairman of the state tax commission may suspend the corporation's right to perform any right acquired by virtue of its status as a corporation. § 27-13-27. Unless and until the suspended corporation is dissolved by an affirmative act of the state (a measure never taken against Bryant), then the corporation, by virtue of its suspension, is "functionally unable to operate though it [does] not cease to exist." . . . . The actual effect of the suspension . . . is that the corporation, although it exists, is deprived of its state-granted power and capacity to function.

Bryant Const., 518 So. 2d at 629.

[221] *Bryant Constr.*, 518 So. 2d at 629.

With respect to the power to sue, the court reasoned that the dismissal prior to the reinstatement of Bryant was "probably correct" since a suspended corporation's lack of power to sue is more a matter of jurisdiction than of the defense of *ultra vires* because the courts of this state cannot recognize suspended corporations as entities that may sue.[224] However, the court ruled that this point was moot since Bryant's amended complaint was filed after reinstatement and section 27-13-27(4) provides that the setting aside of a suspension shall restore all rights to the suspended organization "as though said suspension had not been imposed."[225] Lastly, the court held that the trial court had not considered the merits of Bryant's summary judgment motion thus the Mississippi Supreme Court would not undertake review of that issue. Thereafter the Court reversed and remanded the case for trial.[226]

James A. Bobo

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[222] *Id.*

[223] *Id.* at 630. The court also stated that the defense of *ultra vires*, as raised by Cook Construction, "runs head-on into a brick wall in the form of Miss. Code Ann. § 79-3-11, which provides as follows (with emphasis added):

> § 79-3-11. Defense of *ultra vires*.
>
> *No act of a corporation . . . shall be invalid by reason of the fact that the corporation was without capacity or power to do such act. . . .*

Bryant Constr., 518 So. 2d at 630 (footnotes omitted).

[224] *Bryant Constr.*, 518 So. 2d at 631.

[225] *Id.*

[226] *Id.* at 632.

CRIMINAL LAW

Cases not selected for textual commentary arose in diverse contexts, including admission of confessions,[1] fingerprints,[2] identification,[3] jury instructions,[4] juries,[5] sentencing,[6] and the *Weathersby* rule.[7]

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[1] Coulter v. State, 506 So. 2d 282, 285-86 (Miss. 1987)(after knowing and intelligent waiver of *Miranda* rights, confession is admissible; jury may carry confession into jury room); Johnson v. State, 511 So. 2d 1360, 1366-67 (Miss. 1987)(determination of voluntariness of confession is within discretion of trial judge); Johnson v. State, 512 So. 2d 1246, 1253-54 (Miss. 1987)(where co-defendants are tried in same trial, both of their confessions may be admitted when each confession incriminates only its maker and not another co-defendant); Sims v. State, 512 So. 2d 1256, 1257-58 (Miss. 1987)(findings on voluntariness of confessions will not be reversed absent manifest error of trial judge); Luster v. State, 515 So. 2d 1177, 1179 (Miss. 1987)(first statement of voluntary and unsolicitated confession is admissible without prior *Miranda* warnings; subsequent admissions resulting from interrogatories which are part of "general on-the-scene investigations" are admissible despite absence of prior *Miranda* warnings); Lutes v. State, 517 So. 2d 541, 549 (Miss. 1987)(subject matter of interrogation is not considered in determining voluntariness of statements given after knowing and intelligent waiver).

[2] Giles v. State, 501 So. 2d 406, 408-09 (Miss. 1987)(testimony from state's fingerprint expert and FBI fingerprint card are admissible); Wooten v. State, 513 So. 2d 1251, 1252 (Miss. 1987)(fingerprint evidence alone will not support conviction but fingerprint evidence coupled with other evidence tending to reasonably exclude hypothesis that prints were impressed at any time other than time of crime will support conviction).

[3] Jones v. State, 504 So. 2d 1196, 1198-1200 (Miss. 1987)(pre-trial identification is proper unless it is so impermissibly suggestive as to give rise to substantial likelihood of irreparable misidentification); Davis v. State, 510 So. 2d 794, 795-96 (Miss. 1987)(in-court identification will not be suppressed unless it results from unnecessarily suggestive viewing by witness); White v. State, 507 So. 2d 78, 99-101 (Miss. 1987)(lineup is not unduly suggestive unless from totality of circumstances identification was so impermissibly suggestive as to give rise to very substantial likelihood of irreparable misidentification; victim's in-court identification will not be suppressed as fruit of defendant's unlawful arrest).

[4] Guilbeau v. State, 502 So. 2d 639, 643-44 (Miss. 1987)(trial court is not required to reform inadequate jury instruction or advise counsel of its deficiencies when instruction covers central issue in case already adequately covered in other instructions); Clark v. State, 503 So. 2d 277, 279-80 (Miss. 1987)(flight instruction should only be given where defendant's flight is unexplained and where there is considerable probative value in circumstances surrounding flight); Brazile v. State, 514 So. 2d 325, 326 (Miss. 1987)(reversible error for judge to permit jury instruction which is inaccurate, confusing, and unsupported by evidence at trial); Wright v. State, 512 So. 2d 679, 681-82 (Miss. 1987)(supplemental jury instructions are permitted; instruction to deadlocked jury ordering it to continue its deliberations is within trial judge's discretion); Monroe v. State, 515 So. 2d 860, 863 (Miss. 1987)(lesser included offense instruction may be granted if evidence is sufficient and then only if rational or reasonable jury could find defendant

I. THE *Batson* STANDARD

In 1987, the Mississippi Supreme Court made dramatic changes in

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guilty of said offense and not guilty of principal offense); Fairman v. State, 513 So. 2d 910, 914-15 (Miss. 1987)(jury instructions which are duplicative or which have been withdrawn by defendant need not be given); Williams v. State, 522 So. 2d 201, 208 (Miss. 1987)(defendant has no right to mercy instructions); Crawford v. State, 515 So. 2d 936, 938 (Miss. 1987)(when murder is in issue and defendant fails to object, jury instructions on manslaughter are proper when jury is told all instructions must be considered together); Windham v. State, 520 So. 2d 123, 125-26 (Miss. 1987)(conviction resulting from jury instructions including murder to kill with "deliberate design" and any manslaughter instruction must be reversed as irreconcilable); Russell v. State, 506 So. 2d 974, 976-77 (Miss. 1987)(instruction urging jury to take into consideration youth and capacity of witnesses during their testimony, while improper, is not reversible error); Shoemaker v. State, 506 So. 2d 1193, 1194-95 (Miss. 1987)(unless inflammatory material had harmful effect on jury, judge's instructions will sufficiently cure prejudice resulting from infraction); Koch v. State, 506 So. 2d 269, 271 (Miss. 1987)(request for peremptory instruction of not guilty will be denied unless all evidence supporting state's case as true with reasonable inferences will not support guilty verdict).

[5] Swindle v. State, 502 So. 2d 642, 653-55 (Miss. 1987)(where jury tampering has occurred at trial, sequestration of jury is in interest of justice); Davis v. State, 512 So. 2d 1291, 1292-93 (Miss. 1987)(exception will be made to rule that failure to object to jury before it is impaneled waives right to complain of its composition if juror is suddenly recognized by defense counsel and motion is made for mistrial); Stevens v. State, 513 So. 2d 603, 604-05 (Miss. 1987)(dismissal of juror for good cause and replacement with alternate is within sound discretion of trial judge; failure of juror to respond to question on voir dire does not automatically warrant new trial); Ratliff v. State, 515 So. 2d 877, 879-80 (Miss. 1987)(defendant is not prejudiced when two-thirds of special venire was shown not to be found, defendant must show prejudice in order to attack procedures used by sheriff in summoning special venire).

[6] Watkins v. State, 500 So. 2d 462, 463 (Miss. 1987)(in armed robbery case, trial judge has no authority to impose life sentence without recommendation from jury); Young v. State, 507 So. 2d 48, 50 (Miss. 1987)(during sentencing phase of bifurcated trial, habitual offender statute requires state to prove habitual offender portion of indictment); Dulin v. State, 507 So. 2d 897, 898 (Miss. 1987)(sentence for felonious receipt of stolen property will not be upheld where evidence is insufficient to support finding that value of received stolen property exceeds $100); Bullock v. State, No. DP-14, slip. op. at 664 (Miss. Sept. 2, 1987)(eighth amendment forbids imposition of death penalty on one who aids and abets felony wherein murder is committed by others, but who does not himself kill, attempt to kill, or intend that killing take place or that lethal force will be used; in capital murder cases, court has inherent authority to fix defendant's punishment of life imprisonment if it is deemed necessary and in interest of justice); Slaymaker v. State, 513 So. 2d 921, 922 (Miss. 1987)(trial judge has authority to sentence one convicted of vehicular homicide to imprisonment for up to five years).

[7] Wetz v. State, 503 So. 2d 803, 807-09 (Miss. 1987)(where substantial material evidence contradictory to defendant's story is present in record, it is not reversible error to deny *Weathersby* rule for manslaughter instruction); Alford v. State, 508 So. 2d 1039, 1041 (Miss. 1987)(*Weathersby* instruction may be denied where several eyewitnesses contradict testimony given); Jordan v. State, 513 So. 2d 574, 579 (Miss. 1987)(*Weather-*

the procedures to be used by a minority defendant who objects to the prosecutor's use of peremptory strikes against members of the defendant's race on the venire. The new procedures greatly increase the defendant's ability to successfully challenge his jury panel.

In *Williams v. State*,[8] the black defendant[9] argued that the court erred in denying his motion to quash the jury panel and motion for a new trial, both of which alleged the unconstitutional use by the prosecutor of his peremptory challenges[10] to strike blacks from the jury.[11] Six black persons were on Williams' venire.[12] One was struck by the circuit court for cause; the other five were struck by the prosecutor's peremptory challenges.[13] The prosecutor denied that his strikes were racially motivated, but gave no specific reason for striking the individual jurors.[14] The circuit court denied Williams' motion to quash, citing *Swain v. Alabama*.[15] *Swain*, which was the prevailing law at the time

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sby rule is not available when defendant's statements differ in material particulars from his testimony at trial).

[8] Williams v. State, 507 So. 2d 50 (Miss. 1987).

[9] *Id.* at 51. On January 16, 1986, Williams, a black person, was convicted in the Circuit Court of Harrison County of the armed nighttime burglary of a residence. *Id.*

[10] *Id.* at 52. In a non-capital criminal case, the prosecution and the defense may each challenge peremptorily as many as six prospective jurors. UNIF. CRIM. R. CIR. CT. PRAC. 5.06.

[11] *Williams*, 507 So. 2d at 52.

[12] *Id.* at 51.

[13] *Id.*

[14] *Id.* at 52.

[15] *Id.* Swain v. Alabama, 380 U.S. 202 (1965). In *Swain*, the petitioner, a black man, was convicted of rape in the Circuit Court of Talladega County, Alabama, and was sentenced to death. Throughout his trial, Swain argued that there had been invidious discrimination in the selection of the jurors. *Id.* at 203. Swain asserted that while black males constituted 26% of the males in the county qualified to be grand and petit jurors, only 10-15% of the jury panels from 1953 to 1964 had been black. *Id.* at 205. Moreover, Swain argued that although there had been an average of six to seven blacks on petite jury venires at that time, no black person had actually served on a petite jury for more than 14 years because they were either exempted or struck by the State using peremptory challenges. *Id.* In Swain's trial, eight black persons were on the petit venire yet none were allowed to actually serve because two were exempted and the rest were struck by the prosecution by peremptory challenges. *Id.* The defendant in *Swain* based his argument on Strauder v. West Virginia, 100 U.S. 303 (1879). In *Strauder*, the United States Supreme Court invalidated a state statute which only allowed white people to qualify for jury duty as violative of the fourteenth amendment. 100 U.S. at 310. The *Swain* Court stated that although a black defendant does not have a right to a jury containing black members, "a state's purposeful or deliberate denial to negroes on account of race of participation as jurors in the administration of justice violates the equal protection clause." *Swain*, 380 U.S. at 203-04.

of Williams' trial,[16] required the defendant to show the prosecution's continuous and systematic use of peremptory challenges to exclude members of the defendant's race from the venire.[17] *Swain* had been interpreted to require the defendant to demonstrate a past history of improper use of the state's peremptory challenges in order to successfully object to the prosecutor's strikes in the defendant's own venire.[18] Williams was convicted and appealed to the Mississippi Supreme Court.[19] While his appeal was pending, the United States Supreme Court overturned *Swain* with *Batson v. Kentucky*.[20] With its opinion

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[16] *Williams*, 507 So. 2d at 53. *Swain* had held that a petitioner could not make out a prima facie case merely by alleging the state had discriminated in the use of peremptory challenges. *Swain*, 380 U.S. at 223. Rather, in order to meet the standard announced in *Swain*, the defendant was required to show that a prosecutor, "in case after case, whatever the circumstances may be, is responsible for the removal of negroes who have been selected as qualified jurors by the jury commissions and who have survived challenges for cause, with the result that no negroes ever served on petite juries." *Id.*

[17] *Swain*, 380 U.S. at 227. In *Swain*, the Court stated, "[p]urposeful discrimination may not be assumed or merely asserted . . . it must be proven." *Id.* at 205. *See, e.g.*, Johnson v. State, 487 So. 2d 1195, 1206 (Miss. 1985)(defendant was not denied fair trial even though defendant claimed prosecutor used peremptory challenges to exclude black jurors from jury); Monson v. State, 440 So. 2d 318, 319-20 (Miss. 1985)(presumption that prosecutor used state's challenges to obtain fair and impartial jury is not overcome by allegations of discrimination).

[18] *Williams*, 507 So. 2d at 53. *See* United States v. Boykin, 678 F.2d 1240, 1245 (8th Cir. 1982)(in order to challenge state's use of peremptory strikes, defendant must establish either systematic exclusion of blacks or exclusion for impermissible reason); United States v. Pearson, 448 F.2d 1207, 1213-14 (5th Cir. 1971)(claim of discriminatory use of peremptory challenges cannot be established by proof of government striking negroes in one case); Belino v. State, 465 So. 2d 1043, 1045 (Miss. 1985)(absent anything in record to indicate willful systematic exclusion of black persons from juries, defendant's challenges to peremptory strikes will be denied).

[19] *Williams*, 507 So. 2d at 52.

[20] 476 U.S. 79 (1986). In *Batson*, the petitioner, a black man, was indicted in Kentucky on charges of second degree burglary and receipt of stolen goods. On the first day of trial, the judge conducted voir dire examination of the jury venire and excused certain jurors for cause. Prosecution then used his peremptory challenges to strike all four black persons left on the venire and a jury composed only of white persons was selected. Defense counsel moved to discharge the jury before it was formed, on grounds that the prosecutor's removal of black veniremen violated petitioner's rights under the sixth and fourth amendments to a jury drawn from a cross section of the community. Defendant also argued that his rights to equal protection under the fourteenth amendment had been violated. *Id.* In reviewing this petition, the *Batson* Court stated:

> [T]he state's privilege to strike individual jurors through peremptory challenges is subject to the commands of the Equal Protection Clause . . . [t]he Equal Protection Clause forbids the prosecution to challenge potential jurors solely on account of their race or on the assumption that black jurors as a group will be unable impartially to consider the state's case against a black

in *Williams*, the Mississippi Supreme Court adopted the *Batson* method of determining when a prosecutor has impermissibly excluded veniremen by peremptory challenge.[21] *Williams* holds that a state criminal defendant establishes a prima facie case of impermissible state use of peremptory challenges by showing (1) that he is a member of a cognizable racial group;[22] (2) that the prosecution has used peremptory challenges to strike veniremen of defendant's race; and (3) that "attendant facts and circumstances infer that these challenges were made for the purposes of striking minorities from the jury."[23] If the defendant has made this prima facie showing of purposeful discrimination regarding one or more of the state's peremptory challenges, the prosecutor has the burden to come forward with a racially neutral explanation for those challenges.[24] The court held that the racially neutral reason articulated by the prosecution must be "related to the particular case to be tried,"[25] and stressed that the state's reasons could not include "the prosecutor's assumption — or his intuitive judgment — that they [black jurors] would be partial to the defendant because of their shared race."[26] The defendant may then challenge or rebut the prosecutor's explanations.[27]

In a case[28] decided after Williams' trial but before his appeal, the

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defendant.
Id. at 89.

[21] *Williams*, 507 So. 2d at 52.

[22] *Id.* While the Mississippi Supreme Court did not explain who could be a member of a "cognizable racial group," the *Batson* Court interpreted this phrase to mean that the defendant "must show that he is a member of a racial group capable of being singled out for differential treatment." *Batson*, 476 U.S. at 94. *See* Castaneda v. Partida, 430 U.S. 482, 494 (1977)(defendant's identifiable group is one that is recognizable, distinct and can be singled out for different treatment under the laws).

[23] *Williams*, 507 So. 2d at 52. One of the facts or circumstances on which the defendant is entitled to rely is "the fact, as to which there can be no dispute, that peremptory challenges constitute a jury selection practice that permits 'those to discriminate who are of a mind to discriminate.' " *Id.* (quoting *Batson*, 476 U.S. at 96 (quoting Avery v. Georgia, 345 U.S. 559, 562 (1953)). In considering whether the defendant has made the requisite showing, the *Batson* Court stated that the trial court should consider all relevant circumstances. *Batson*, 476 U.S. at 96-97. The Court noted that "a 'pattern' of strikes against black jurors included in a particular venire might give rise to an inference of discrimination during voir dire examination and in exercising his challenges may support or refute an inference of discriminatory purpose." 476 U.S. at 97.

[24] *Williams*, 507 So. 2d at 52.

[25] *Id.* (quoting *Batson*, 476 U.S. at 98).

[26] *Id.* Yet the prosecutor's explanation need not be one which would justify a challenge for cause. *Id.*

[27] *Id.* at 53.

[28] Griffith v. Kentucky, ____ U.S. ____, 107 S. Ct. 708 (1986). In *Griffith*, the Su-

United States Supreme Court held that *Batson* applied retroactively to those cases which were pending on direct review,[29] or not yet final,[30]

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preme Court consolidated two cases. The first defendant, Randall Lamont Griffith, a black man, was convicted of first degree robbery and theft by unlawful taking. On the first day of trial, after voir dire, the prosecution used four of its challenges to strike four of the five prospective black jurors. The only black remaining on the venire was subsequently removed by the trial court. Defense counsel, objecting to the prosecutor's strikes, asked the Court to require the prosecutor to explain his reasons for using the peremptory strikes against the four black veniremen. Defense's request was denied, and defendant's counsel then moved to discharge the panel, alleging that the prosecutor's use of peremptory challenges constituted a violation of the sixth and fourteenth amendments. The court denied the motion and the jury convicted the defendant of first degree robbery. Griffith was sentenced to ten years' imprisonment, which was subsequently lengthened to 20 years, according to a persistent felony statute, 16A KY. REV. STAT. § 537,080 (1985). The Supreme Court of Kentucky affirmed based on *Swain.* Griffith filed a petition on writ of certiorari. While his petition was pending, the U.S. Supreme Court decided *Batson.*

The second defendant, Willie Davis, a black man, was convicted by a jury in the U.S. District Court for the Western District of Oklahoma on narcotics charges. During jury selection, two venire panels were assembled, which included six prospective black jurors. Four blacks were excused for cause by the court and the other two were excused by the prosecutor's use of peremptory challenges. Although defendant's counsel objected to the prosecutor's actions, claiming that the petitioner was thereby denied the jury representative of his community, the objection was denied. When the second venire was being impaneled, the prosecution asked the jury clerk about the racial composition of the venire. At a later hearing, there was evidence that the prosecutor said to the clerk that he would like to have very few blacks on the panel. The trial court concluded that a new trial would not be necessary if the jury convicted the petitioner. The U.S. Court of Appeals for the Tenth Circuit affirmed. United States v. Brown, 770 F.2d 912 (10th Cir. 1985). Prior to *Batson*, petitioner timely filed a petition for writ of certiorari which was granted by the Supreme Court. 476 U.S. 1157 (1986). In both cases, the Supreme Court limited review to the question whether the *Batson* analysis applied retroactively to state or federal convictions pending on direct review at the time *Batson* was decided.

[29] In Caldwell v. State, 517 So. 2d 1360 (Miss. 1987), the defendant's earlier conviction of capital murder and sentence of death had been affirmed on direct appeal by the Mississippi Supreme Court. Caldwell v. State, 443 So. 2d 806 (Miss. 1983). The U.S. Supreme Court vacated his sentence and remanded for resentencing. Caldwell v. Mississippi, 472 U.S. 320 (1985). Defendant then sought post-conviction relief in the state courts, contending that the prosecutor's use of peremptory challenges to strike all blacks from the venire was unconstitutional. Caldwell v. State, 481 So. 2d 850, 851 (Miss. 1985). The Mississippi Supreme Court rejected this claim, citing *Swain.* Defendant filed a petition for certiorari with the United States Supreme Court on March 3, 1986, and on April 30, 1986, *Batson* was decided. Caldwell v. State, 517 So. 2d at 1361. On remand to consider Caldwell's *Batson* claim, the Mississippi Supreme Court held that Caldwell's petition for certiorari was collateral, not direct, review and therefore his jury selection procedure was not subject to *Batson* review. *Id.* at 1361.

[30] *Griffith*, 107 S. Ct. at 712 n.6. According to *Griffith*, a case is "final" where, "the judgment of conviction has been rendered, the availability of direct appeal exhausted,

when *Batson* was decided.[31] Because Williams had timely objected to the prosecutor's strikes, he qualified for retroactive *Batson* analysis of his jury panel.[32] The court noted that Williams had made out a prima facie case, and that the prosecutor's stated justification for his strikes was insufficient to satisfy the *Batson* standard.[33] However, the court said that the prosecutor's justification might have satisfied the *Swain* standard as it existed at the time of Williams' trial, and that the prosecutor could not have anticipated the change in standards.[34] The court held that "the prosecution may not fairly be said to have waived the opportunity to do that which it had no reason to know it was obligated to do"[35] and remanded the case to the circuit court to give the prosecutor an opportunity to come forward with *Batson*-conforming, non-racial explanations for each of the peremptory strikes he used on black veniremen.[36] Furthermore, in *Thomas v. State*,[37] the court held that failure to make a timely objection to the state's peremptory challenges completely bars any later attempt to bring a *Batson* claim on appeal.[38]

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and the time for the filing of a petition for certiorari elapsed or a petition for certiorari finally denied." *Id.*

[31] *Id.* at 708. The *Griffith* Court reasoned, "the nature of judicial review requires that we adjudicate specific cases, and each case usually becomes a vehicle for announcement of a new rule. But after we have decided a new rule and the case selected, the integrity of judicial review requires that we apply the rule to all similar cases pending on direct review." *Id.* at 713.

[32] *Williams*, 507 So. 2d at 53. The *Williams* court stated that *Batson* was applicable to Williams' case since Williams had perfected his appeal two months before *Batson* and his conviction had not yet become final when *Batson* was decided. *Id.*

[33] *Id.* In *Williams*, after defense objected to the prosecutor's strikes, the state responded: "The state denies systematically excluding blacks in this trial from that jury panel and the record should also reflect the state used a peremptory challenge on an individual male who was white." *Id.*

[34] *Id.*

[35] *Id.*

[36] *Id.* The *Williams* court noted the difficulty a busy trial lawyer would have recalling specific reasons for striking potential jurors in a case from several years ago. *Id.*

[37] 517 So. 2d 1285 (Miss. 1987). Elisha Thomas, Jr. was convicted of rape and was subsequently sentenced to 15 years imprisonment. At trial, the state used two of its peremptory challenges to strike blacks from the venire. Thomas did not object to the use of these peremptory challenges, nor did he move to strike the jury venire. His first objection to the jury panel came in a motion for judgment notwithstanding the verdict, or in the alternative, a motion for a new trial. These motions were denied. *Id.* at 1285-86. In an unsuccessful appeal, Thomas did not allege racial discrimination in jury selection. *Id.* at 1286. Because his appeal was pending on direct review when *Batson* was decided, the selection of his jury was subject to *Batson* review. *Id.* at 1285-86.

[38] *Id.* The court explained that while the *Batson* opinion did not expressly address the issue of timely objection, the *Batson* opinion "contemplates" a timely question. *Id.* Foreshadowing of the holding in *Thomas* may be seen in Harper v. State, 510 So. 2d 530

The court relied on *Irving v. State*,[39] wherein a defendant's failure to make a contemporaneous objection to the racial composition of the jury was held to have waived his right to assert a claim of improper use of peremptory challenges.[40] The *Thomas* court observed that Mississippi has long followed the contemporaneous objection rule,[41] and noted that the Fifth Circuit Court of Appeals[42] and state courts[43] had predicated *Batson* scrutiny on some form of timely objection.[44] The court ruled that for a *Batson* objection to be timely, it must be made prior to the impaneling of the jury.[45]

A strongly worded dissent argued that the timely objection rule should not apply to cases tried before *Batson* was decided.[46] The dissent argued that although the contemporaneous objection rule was useful, it ought not bar a defendant from asserting rights which were not

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(Miss. 1987). At Harper's trial the prosecutor used peremptory challenges to eliminate all blacks from the venire. *Id.* at 531. Defense counsel objected to these strikes in his motion to quash the jury panel and his motion for new trial, both of which were denied. *Id.* *Batson* was decided while *Harper* was on direct appeal. *Id.* at 532. In remanding the case to the lower court for a *Batson* hearing, a unanimous court noted that "the question was timely raised at jury selection by a motion to quash the jury on the grounds of systematic exclusion, and was urged again on motion for new trial. Therefore, the *Batson* principle applies in this case." *Id.*

[39] 498 So. 2d 305 (Miss. 1986).

[40] *Thomas*, 517 So. 2d at 1286.

[41] *Id.* at 1286-87. *See* Copeland v. State, 423 So. 2d 1333, 1333-35 (Miss. 1982)(no objection made at trial which would have alerted judge and given prosecution opportunity to justify); Fermo v. State, 370 So. 2d 930, 935 (Miss. 1979)(post-trial objection to jury foreman barred as untimely); Arnold v. State, 171 Miss. 164, 165, 157 So. 247, 248 (1934)(failure to timely object to jury panel acts as waiver).

[42] *Thomas*, 517 So. 2d at 1287. *See* United States v. Erwin, 793 F.2d 656, 667 (5th Cir. 1986)(motion to strike jury after venire was released was untimely); Government of the Virgin Islands v. Forte, 806 F.2d 73, 75-76 (3d Cir. 1986)(*Batson* objection first raised on motion for new trial is untimely).

[43] *Thomas*, 517 So. 2d at 1287. *See*, Price v. State, 726 S.W.2d 611, 613 (Tex. Ct. App. 1987)(objection is untimely if not made before venire is dismissed).

[44] *Thomas*, 517 So. 2d at 1287.

[45] *Id.* at 1287-88. See also Jones v. State, 517 So. 2d 1295 (Miss. 1987), where the court explained that in cases tried prior to *Batson*, the timely objection must have been grounded on allegations of racially discriminatory jury selection. *Id.* at 1311. The court noted that a timely objection on *Swain* grounds would have been sufficient to preserve a challenge to the jury panel for later *Batson* review. *Id.*

In Joseph v. State, 516 So. 2d 505 (Miss. 1987), another pre-*Batson* case, the defendant timely objected and demanded racially neutral explanations for the prosecutor's peremptory strikes. *Id.* Indeed, defendant cited the then pending United States Supreme Court case of *Batson* in making her objection. *Id.* The Mississippi Supreme Court remanded *Joseph* for a *Batson* hearing. *Id.*

[46] *Thomas*, 517 So. 2d at 1288-95 (Robertson, J., dissenting).

available at the time of trial.[47] " '[O]nce it is seen that, with respect to a particular category of constitutionally protected rights, there is no meaningful opportunity for vindication at the trial court level, surely the state's interest in judicial efficiency manifest in its contemporaneous objection rule or its procedural bar is stalemated and loses its force.' "[48] The dissent noted that the court had earlier refused to hold that a prosecutor had waived his right to assert racially neutral explanations for his peremptory challenges in a pre-*Batson* trial.[49] Likewise, argued the dissent, the defendant ought not to be found to have waived *Batson* rights which did not exist at the moment of waiver.[50] Distinguishing *Thomas* from *Irving*, the dissent noted that *Irving* had been decided before *Batson* had been made retroactive.[51]

Mississippi's adherence to the *Batson* standards is a step forward for minority defendants. However, limiting the cases to be "Batsonized" to those in which objections were timely made diminishes the positive effect of *Williams*.[52] Although the contemporaneous objection rule is necessary to protect the integrity of decisions made at the original trial,[53] it should not outweigh the defendant's ability to assert his right to a fair jury panel chosen without racial discrimination. It is apparent that before *Batson* was decided no one could have expected that *Batson* type challenges would be effective.[54] By limiting the cases which may be remedied by *Batson*, the court greatly impairs an important rule which guarantees to every defendant equal protection.

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[47] *Id.* The dissent noted two reasons for the contemporaneous objection rule. "Sandbagging" is prevented by requiring that the opposing party be given notice of an objection and an opportunity to counter-argue or take curative action. *Id.* at 1290. The other purpose of the rule is to protect judicial resources by giving a trial judge the chance to correct his errors. *Id.* The dissent argued that even had the defendant made a *Swain* objection at trial, it would have been overruled by the trial judge. *Id.* Clearly the defendant could not have sandbagged the prosecution by withholding a *Batson* objection: "no one foresaw *Batson* enough to sandbag." *Id.* Also the trial judge could not "correct his own errors" when, before *Batson*, it was not error to overrule defendant's *Swain* objection. *Id.* Therefore, argued the dissent, "application [of the rule] to bar assertion of rights which at trial had no existence is seen as only folly." *Id.* at 1289.

[48] *Id.* (quoting Read v. State, 430 So. 2d 832, 841 (Miss. 1983)).

[49] *Id.* at 1289-92. *See Williams, supra*, 507 So. 2d at 53 (before *Batson*, prosecutor had no way of knowing what was required of him).

[50] *Thomas*, 517 So. 2d at 1289-92. "If the defendant did not know, and had no means of knowing he had the right, how could he voluntarily waive it?" *Id.* at 1292.

[51] *Id.* at 1292.

[52] *See supra* note 22.

[53] *See supra* notes 34-37.

[54] *See supra* notes 39-43.

II. Discovery Requirements

In 1987, the Mississippi Supreme Court handed down several cases which indicate that state prosecutors are having continued difficulty in complying with the discovery requirements of Rule 4.06 of Mississippi Uniform Criminal Rules of Circuit Court Practice.[55]

In *Turner v. State*,[56] the defendant filed a discovery request pursuant to Rule 4.06 at least eighteen months before trial, seeking, *inter alia*, the names and addresses of any confidential informants.[57] Rule 4.06(2) of the Mississippi Uniform Criminal Rules of Circuit Court Practice requires the disclosure of an informant who is an "eyewitness to the event or events constituting the charge against defendant."[58] Although the defendant's discovery request automatically required the State to provide the name of any such informant,[59] the State failed to do so.[60] At trial, it became apparent that there was a confidential informant who had in fact been a witness to the defendant's alleged drug transaction.[61] Defense counsel timely moved[62] for a continuance,[63] but the trial court denied the motion.[64]

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[55] The following are discovery cases which do not merit extended discussion: Shaw v. State, 521 So. 2d 1278, 1282 (Miss. 1987)(failure to make timely objection will foreclose defendant's opportunity for continuance to examine evidence); Nixon v. State, No. 57177, slip op. at 2709 (Miss. Dec. 9, 1987)(failure to make timely objections will foreclose opportunity to raise discovery violations); Gallion v. State, 527 So. 2d 1364, 1372-73 (Miss. 1987)(previously undisclosed photographs made from surveillance camera may be used in state's rebuttal).

[56] 501 So. 2d 350 (Miss. 1987). Defendant was convicted in Harrison County for the sale of a controlled substance. Miss. Code Ann. § 41-29-115(d)(b) (Supp. 1986). Part of the alleged transaction was witnessed by a confidential informant. *Turner*, 501 So. 2d at 350-51.

[57] *Turner*, 501 So. 2d at 351-52.

[58] Miss. Unif. Crim. R. Cir. Ct. Prac 4.06(2).

[59] *Turner*, 501 So. 2d at 352. In Stewart v. State, 512 So. 2d 889 (Miss. 1987), the supreme court held that once a defendant makes a request under Rule 4.06, the prosecutor is obligated to provide discovery, and this obligation does not depend on any efforts by defendant to further enforce his right to discovery. *Id.* at 891. The supreme court specifically rejected the trial court's contention that defendant was obliged to press his motion for discovery at the court's regular motion day. *Id.* The trial court refused defendant's motion for continuance even though the prosecutor made no disclosure until the day before trial. *Id.* Included in this tardy disclosure was a copy of defendant's statement to the police, a copy of his consent to search form, a copy of the return from the search, a copy of defendant's waiver of rights, the state's witness list, hospital records from the alleged victim and photos of the identification lineup. *Id.* at 893. Based on the State's failure to provide timely discovery, the supreme court was "unable to say with confidence" that denial of Stewart's motion for continuance was harmless error, and therefore reversed his conviction and remanded. *Id.* at 892-93.

[60] *Turner*, 501 So. 2d at 352. *See* Ray v. State, 503 So. 2d 222, 224 (Miss. 1987)(name of confidential informant who participates in or witnesses crime ordinarily must be disclosed); Breckenridge v. State, 472 So. 2d 373, 377 (Miss. 1985)(court erred in failing to disclose confidential informant). *But cf.* Watson v. State, 433 So. 2d 1142,

The Mississippi Supreme Court reversed and remanded, citing the denial of the motion for continuance as error.[65] The court held that because the State had not responded to defendant's request for discovery, the defense was entitled to a continuance when it learned for the first time, at trial, of discoverable information.[66] The court held that

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1144-45 (Miss. 1983)(where confidential informant's testimony is not relevant or material, his identity need not be disclosed).

[61] *Turner*, 501 So. 2d at 352.

[62] *Id.* In Robinson v. State, 508 So. 2d 1067 (Miss. 1987), the court held that a defendant who has filed a discovery request must object to the introduction of newly produced, discoverable evidence at trial. Upon timely objection, the trial court should give defense counsel an opportunity to examine the evidence and to determine if he wishes to ask for a continuance. *Id.* at 1070.

The *Robinson* court stated, "Disclosure is the hallmark of fairness and the quest for justice that should be the goal of the criminal justice system." *Id. Accord* Hall v. State, 490 So. 2d 858, 859 (Miss. 1986)(even though physical evidence was not introduced at trial, state is required to disclose all evidence where testimony from arresting officer refers to such evidence at trial); Hentz v. State, 489 So. 2d 1386, 1388 (Miss. 1986)(all exculpatory material held by state must be available to defendant before trial).

[63] *Turner*, 501 So. 2d at 352.

[64] *Id.* The court noted that the trial judge apparently recognized the prosecutor's violation of Rule 4.06. However, upon learning that the prosecutor had lost contact with the informant some ten months earlier, the trial court denied the continuance on the ground that it would be useless. *Id.*

[65] *Id.* at 352-53.

[66] *Id.* The court held that although the prosecutor did not know where the informant could be found, the defendant was entitled to an opportunity to use his own resources to locate her. *Id.*

In Inman v. State, 515 So. 2d 1150 (Miss. 1987), the defendant moved for a continuance on the ground that, although he had filed a Rule 4.06 discovery motion, he was not told about two state witnesses until the day before trial. The supreme court reversed and remanded, citing the trial court's denial of the motion. *Id.* at 1153-54. While holding that a continuance is required, the court stressed that in many cases a postponement of one or two days, or in some circumstances, even an hour or two, would give the defendant sufficient opportunity to make use of the newly furnished information. *Id.* at 1153 (citing Foster v. State, 484 So. 2d 1009, 1011 (Miss. 1986)).

In Moore v. State, 508 So. 2d 666 (Miss. 1987), the defendant was charged with manufacturing a controlled substance (growing marijuana). MISS. CODE ANN. § 41-29-113 (1972). Although he had filed a Rule 4.06 discovery motion, the State was allowed to introduce, over timely objection, a previously undisclosed statement made by defendant to police. ("I don't know what to say when you can't grow a little homegrown.") *Moore*, 508 So. 2d at 667-68. The court acknowledged that the defendant's oral, inculpatory statement made to the police was discoverable, yet the court declined to reverse defendant's conviction. *Id.* at 668. The court's only explanation was "we find [the statement] the defense must be given a "meaningful opportunity" to make use of discoverable information.

The 1987 discovery cases graphically illustrate the importance of Rule 4.06. Generally, unless the rule is complied with, a defendant's case will be reversed notwithstanding evidence which clearly implicates the defendant.[67] These decisions stress the court's willingness to go to great lengths to enforce a rule which should be complied with easily.[68] The essential purpose of Rule 4.06 is to eliminate ambushing or surprising a defendant at trial.[69] By strictly scrutinizing discovery violations, and reversing cases even where the overwhelming weight of evidence supports a guilty verdict, the Mississippi Supreme Court protects a criminal defendant's right to a fair and equitable trial.

III. EVIDENCE

Numerous decisions relating to evidence in the area of criminal law were rendered by the Mississippi Supreme Court in 1987.[70] In *Jen-*

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was sufficiently innocuous to not rise to reversible proportions." *Id.* at 668. Perhaps the court felt that in this particular instance, one or two minutes was sufficient opportunity for defense counsel to digest and utilize the newly disclosed statement.

In Wells v. State, 521 So. 2d 1274 (Miss. 1987), the court specifically held that "the state's failure to disclose an oral statement by a defendant which was neither an admission of guilt nor inconsistent with his asserted defense was not reversible error even though there was a violation of Rule 4.06." *Id.* at 1276 (quoting Boches v. State, 506 So. 2d 254, 262 (Miss. 1987)).

[67] *See supra* note 59.

[68] *See supra* note 56.

[69] *See supra* note 59.

[70] The Mississippi Supreme Court decided the following cases relating to evidence in the area of criminal law which are not treated textually: Hooker v. State, 516 So. 2d 1349, 1352 (Miss. 1987)(testimony which is statement against interest of unavailable witness is exception to hearsay rule); Wilson v. State, 515 So. 2d 1181, 1182 (Miss. 1987)(in sexual crimes, testimony by third party regarding substantially similar prior sexual acts committed by defendant with same person is admissible); Murriel v. State, 515 So. 2d 952, 956 (Miss. 1987) (evidence at rape trial of unrelated abortion is highly prejudicial, increases risk of jury confusion, and places undue burden on defendant); Pulliam v. State, 515 So. 2d 945, 947 (Miss. 1987) (where there is doubt as to relevancy of evidence, it should be admitted); Clark v. State, 514 So. 2d 1221, 1223-24 (Miss. 1987) (it is error for trial court to exclude testimony as being irrelevant where testimony tends to disprove fact in issue); Rawls v. State, 513 So. 2d 942, 944 (Miss. 1987) (where defendant's sole connection with burglary is that he was seen at time when burglars were fleeing scene, evidence is insufficient to support conviction); Shaw v. State, 513 So. 2d 916, 919 (Miss. 1987) (evidence of other crimes separate and distinct from that charged in indictment is admissible to prove motive, intent, preparation and plan); Crenshaw v. State, 513 So. 2d 898, 899 (Miss. 1987) (videotapes are admissible into evidence); Parks v. State, 522 So. 2d 755, 756 (Miss. 1987)(evidence of second crime is inadmissible unless it comes within

kins v. State,[71] the Mississippi Supreme Court construed the relevancy provisions of the new Mississippi Rules of Evidence. Douglas Jerome Jenkins was charged with the attempted kidnapping of Ira Kynerd.[72] Jenkins filed a motion in limine prior to trial seeking to prohibit the state from introducing evidence that Jenkins and another man on the same day had planned a robbery which was never committed.[73] This motion was overruled by the trial judge.[74] At trial, the prosecution offered Jenkins' confession that he and two others had planned to rob a grocery store, but inexplicably performed no robbery.[75] Jenkins was subsequently found guilty of attempted kidnapping and sentenced to

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narrowly defined exceptions); Collins v. State, No. 56,926 (Miss. Aug. 26, 1987) (it is highly inflammatory, irrelevant, and outside scope of res gestae to introduce "girlie" magazines into evidence in sexual battery suit where magazines were found on premises of offender but were not actually shown to victims); Montgomery v. State, 515 So. 2d 845, 848 (Miss. 1987) (where state's case is based entirely upon circumstantial evidence, state is required to prove defendant guilty not only beyond reasonable doubt, but to exclusion of every reasonable hypothesis consistent with innocence); Tolbert v. State, 511 So. 2d 1368, 1372-73 (Miss. 1987) (where prosecution has not acted in bad faith in losing piece of evidence, and where value of such evidence is not apparent before its destruction, then no prejudice results therefrom); Whitley v. State, 511 So. 2d 929, 931-32 (Miss. 1987) (where there is probable cause for arrest and submission to blood alcohol test, such test is admissible into evidence); McFee v. State, 511 So. 2d 130, 134-35 (Miss. 1987) (where defendant is convicted of rape, admission of evidence of victim's subsequent death, introduced through photographs of victim's body and statements of prosecution and its witnesses, is not per se error if such evidence is sufficiently relevant and otherwise admissible); Elmore v. State, 510 So. 2d 127, 131 (Miss. 1987) (it is error for trial court to admit testimony of third party regarding unconvicted prior sexual crimes for which defendant was not on trial); Ray v. State, 503 So. 2d 222, 225 (Miss. 1987)(where no predicate has been laid by showing that defendant signed or provided specific information contained in a notice of alibi, such notice cannot be used by prosecution as impeachment or rebuttal evidence); Boches v. State, 506 So. 2d 254, 261 (Miss. 1987) (intent of Legislature is to allow Mississippi courts to prosecute criminal acts that occur within Mississippi whether or not they begin or were intended to end in Mississippi); Hecklar v. State, 503 So. 2d 269, 270 (Miss. 1987) (where it was determined in previous case that Marie Hill qualified as handwriting expert, it was reversible error for trial court to disallow her testimony as such); Higgins v. State, 502 So. 2d 332, 335 (Miss. 1987) (it is harmless error to allow testimony that defendant was silent after being read his *Miranda* rights); McLean v. State, 502 So. 2d 651, 651 (Miss. 1987) (testimony of addictologist ruled inadmissible); Fielder v. State, 500 So. 2d 1002, 1004 (Miss. 1987) (it is unnecessary to refile motion to suppress at second trial where mistrial is declared at first trial and trial is continued in next term of court).

[71] 507 So. 2d 89 (Miss. 1987).

[72] *Id.* at 90.

[73] *Id.*

[74] *Id.*

[75] *Id.*

ten years imprisonment.[76]

On review, the supreme court considered whether the evidence of Jenkins' prior intention of robbing the grocery store was admissible in Jenkins' trial for attempted kidnapping.[77] The court stated that the proper consideration, in light of Rules 401[78] and 402,[79] of the Mississippi Rules of Evidence was whether the evidence of the aborted robbery would have "the tendency to make the existence of any fact that is of consequence to the determination of whether Jenkins was guilty of the attempted kidnapping of Ira Kynerd more probable or less probable than it would have been without the evidence."[80] In this context, the court determined that the attempted kidnapping was rendered more probable by the introduction of the evidence pertaining to the planned grocery robbery, since common sense dictates that one who fails in attempting to commit one crime is likely to commit another.[81] However, the supreme court stated that although the evidence indicated that Jenkins was more likely to commit the crime because he had previously formed the intent to rob the grocery, such evidence would be inadmissible under Rule 403, since its probative value was outweighed by its prejudicial effect.[82] Therefore, since the evidence was prejudicial under Rule 403, it would not be admissible under Rules 401 and 402 to show that it was more probable that Jenkins was guilty of attempted kidnapping.[83]

Although the evidence was inadmissible under Rule 403, the court concluded that the evidence would be admissible under Rule 404(b), since the fact that Jenkins and his accomplice went to the grocery to commit a robbery was relevant to the issues of motive, opportunity and intent to participate in the kidnapping of Kynerd.[84] The supreme court noted that the critical factor was the purpose of the kidnapping — the robbery of Kynerd.[85] In this light, the evidence of the aborted grocery robbery was relevant to the issues of motive, opportunity and intent to commit the attempted kidnapping.[86] Furthermore, evidence which is otherwise admissible under Rule 404(b) must still withstand the prejudice test set forth in Rule 403.[87] In conclusion, the supreme court held that since the Rule 403 balancing test is one of judgment, the lower court's decision to admit the evidence was not an abuse of judicial discretion.[88] Finding the assignments of error without merit, the Mississippi Supreme Court affirmed.[89]

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[76] *Id.*

[77] *Id.* at 91.

[78] *Id.* Rule 401 provides: " 'Relevant Evidence' means evidence having any tendency to make the existence of any fact that is of consequence to the determination of the action more probable or less probable than it would without the evidence." MISS. R. EVID. 401.

[79] *Jenkins*, 507 So. 2d at 91. Rule 402 provides: "All relevant evidence is admissible except as otherwise provided by the Constitution of the United States, the Constitution of the State of Mississippi or by these rules. Evidence which is not relevant is not admissible." MISS. R. EVID. 402.

[80] *Jenkins*, 507 So. 2d at 91.

[81] *Id.* at 92.

[82] *Id.* Rule 403 provides: "Although relevant, evidence may be excluded if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, ..." MISS. R. EVID. 403.

[83] *Jenkins*, 507 So. 2d at 91.

Continuing the interpretation of the new Mississippi Rules of Evidence, the supreme court decided *Cummins v. State*.[90] Billy Cummins, a Sunflower County supervisor, was convicted of receiving stolen chemicals on March 23, 1987.[91] On appeal, Cummins argued that hearsay statements were improperly admitted into evidence at trial.[92] Having unsuccessfully attempted to obtain the subpoena of Cummins' son two days before trial, the state served notice pursuant to Rule 803(24) of the Mississippi Rules of Evidence[93] that it intended to introduce an

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[84] *Id.* at 93. Rule 404(b) provides: "Evidence of other crimes, wrongs, or acts is not admissible to prove the character of a person in order to show that he acted in conformity therewith. It may, however, be admissible for other purposes such as proof of motive, opportunity, intent, preparation, plan, knowledge, identity, or absence of mistake or accident." Miss. R. Evid. 404(b).

[85] *Jenkins*, 507 So. 2d at 93.

[86] *Id.*

[87] *Id.*

[88] *Id.*

[89] *Id.*

[90] 515 So. 2d 869 (Miss. 1987).

[91] *Id.* at 871.

[92] *Id.* at 873.

[93] *Id.* at 872. Rule 803(24) provides:

> The following are not excluded by the hearsay rule, even though the declarant is available as a witness:
>
> (24) *Other exceptions.* A statement not specifically covered by any of the foregoing exceptions but having equivalent circumstantial guarantees of trustworthiness, if the court determines that (A) the statement is offered as evidence of a material fact; (B) the statement is more probative on the point for which it is offered than any other evidence which the proponent can procure through reasonable efforts; and (C) the general purpose of these rules and the interest of justice will be served by admission of the statement into evidence. However, a statement may not be admitted under this exception unless the proponent of it makes known to the adverse party sufficiently in advance of the trial or hearing to provide the adverse party with a fair opportunity to prepare to meet it,

oral statement made by Cummins' son: "I told daddy not to fool with that damned man, Ray Thomas. I used some of the chemicals, do you want me to replace them?"[94] The trial judge admitted the statement into evidence through Robert Malone, the state's rebuttal witness.[95] Cummins asserted that the hearsay testimony was erroneously admitted, thereby denying him a fair trial.[96]

Addressing the assignment of error, the Mississippi Supreme Court stated:

> Before any evidence may be admitted under the residual exceptions to the hearsay rule the following conditions must be met. They are:
> (1) The proponent of the evidence must give the adverse party the notice specified within the rule.
> (2) The statement must have circumstantial guarantees of trustworthiness equivalent to the 23 specified exceptions listed in Rule 803.
> (3) The statement must be offered as evidence of a material fact.
> (4) The statement must be more probative on the point for which it is offered than any other evidence the proponent can procure through reasonable efforts.
> (5) The general purpose of the Federal Rules [sic] and the interests of justice must best be served by admission of the statement into evidence.[97]

The supreme court then analyzed each of the conditions as applied to the facts of the case.[98] First, the court concluded that giving notice one day before trial was insufficient to provide the defendant a fair opportunity to challenge the admissibility of the statement.[99] The second

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> his intention to offer the statement and the particulars of it, including the name and address of the declarant.

MISS. R. EVID. 803(24).

[94] *Cummins*, 515 So. 2d at 872-73.

[95] *Id.* at 873.

[96] *Id.*

[97] *Id.* The supreme court cited United States v. Mathis, 559 F.2d 294 (5th Cir. 1977), as authority for the test under Rule 803(24). *Cummins*, 575 So. 2d at 873; *see also* United States v. Guevara, 598 F.2d 1094, 1100 (7th Cir. 1979) (under identical federal rule, courts require specific findings from analysis to be made part of record).

[98] *Cummins*, 515 So. 2d at 873-75.

[99] *Id.* at 874; *see* United States v. Mathis, 559 F.2d 294, 299 (5th Cir. 1977) (notice should be given sufficiently in advance of trial so as to provide opposing party with fair opportunity to meet it); *cf.* United States v. One 1968 Piper Navajo Engine Aircraft, 594

condition failed since the state offered no evidence establishing the trustworthiness of the statements.[100] Regarding the third condition, the court found that "[w]hether the chemicals were used by a member of Cummins' family was certainly a material issue."[101] Fourth, the state failed to use reasonable efforts since it waited until two days before trial to attempt to procure the attendance of Cummins' son.[102] Finally, the supreme court determined that the admission of testimony was not in the interest of justice, nor did it serve the purposes of the Mississippi Rules.[103] Since Cummins was denied a fair trial, the supreme court reversed.[104]

The final case interpreting the Mississippi Rules of Evidence rendered by the Mississippi Supreme Court in 1987 was *Peterson v. State*.[105] Henry Peterson was convicted of selling marijuana to narcotics agent Donna Conner.[106] On appeal, Peterson argued that evidence of a prior felony conviction was admitted over objection and in contravention of Rule 609(a) of the Mississippi Rules of Evidence.[107] At trial, defense counsel objected to the introduction of the evidence "under the New Rules of Civil Procedure."[108]

F.2d 1040, 1041 (5th Cir. 1979) (trial judge is given great latitude in determining whether notice was sufficient). *But see* United States v. Ruffin, 575 F.2d 346, 358 (2d Cir. 1978) (applying rigid standard in determining whether notice was sufficient). The Mississippi Supreme Court also concluded that the hearsay evidence offered at trial exceeded the scope of the notice given to the defendant. *Cummins*, 515 So. 2d at 874.

[100] *Cummins*, 515 So. 2d at 874; *see also* United States v. Ruppel, 666 F.2d 261, 271 (5th Cir. 1982) (evidence must have "circumstantial guarantees of trustworthiness"); *cf.* Herdman v. Smith, 707 F.2d 839, 842 (5th Cir. 1983) (need for evidence must be balanced against trustworthiness); United States v. White, 611 F.2d 531, 538 (5th Cir. 1980) (same). *See generally* 4 J. WEINSTEIN, EVIDENCE 803-76 (1985) (other factors to consider in analyzing whether evidence should be admitted).

[101] *Cummins*, 515 So. 2d at 875.

[102] *Id.* at 874; *see also* Byrd v. Hunt Tool Shipyards, Inc., 650 F.2d 44, 46 (5th Cir. 1981) (evidence must be more probative on point than any other evidence that proponent can procure through reasonable efforts); Huff v. White Motor Corp., 609 F.2d 286, 294 (7th Cir. 1979) (same).

[103] *Cummins*, 515 So. 2d at 875; *see also* MISS. R. EVID. 102 (1986) (outlining purposes of rules). The supreme court noted, citing Miller v. State, 473 So. 2d 945 (Miss. 1985), that the evidence may have implicated the confrontation clause even if it was admissible under Rule 803(24). *Cummins*, 515 So. 2d at 875.

[104] *Cummins*, 515 So. 2d at 877. The court also found reversible error when the prosecution suppressed material evidence regarding facts alleged in the indictment. *Id.* at 876.

[105] 518 So. 2d 632 (Miss. 1987).

[106] *Id.* at 634.

[107] *Id.*

[108] *Id.* at 635.

The first issue addressed by the Mississippi Supreme Court was whether the objection was sufficient under Rule 103(a)(1) of the Mississippi Rules of Evidence.[109] Rule 103 requires that a specific ground for the objection must be stated, unless the ground is otherwise apparent from the context.[110] The supreme court concluded that since it was apparent from the context of the objection that defense counsel was objecting to the admissibility of the prior conviction, then the assignment was not procedurally barred.[111]

Turning to the substance of the assignment, the court analyzed whether the evidence was admissible under Rule 609(a)(1).[112] Since Rule 609(a)(1) requires the trial judge to determine whether the probative value of admitting the evidence of a witness' prior felony conviction outweighs its prejudicial effect,[113] the question became whether such determination must be made on the record.[114] The supreme court adopted the Fifth Circuit rule under the Federal Rules of Evidence[115] and held that the trial judge must make an on-the-record determination of the probative value of the evidence.[116] In order to provide guidance to the trial court in making its determination on the record,[117] the supreme court listed five specific factors to consider: "(1) The impeachment value of the prior crime. (2) The point in time of the conviction and the witness' subsequent history. (3) The similarity between the past crime and the charged crime. (4) The importance of the defendant's testimony. (5) The centrality of the credibility issue."[118] Applying the factors to the facts of the instant case, the court concluded that the prejudicial effect of the evidence outweighed the probative value.[119] Therefore, having found error at the trial below, the supreme court reversed and remanded.[120]

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[109] *Id.* Rule 103(a)(1) provides:

> (a) Effect of Erroneous Ruling. Error may not be predicated upon a ruling which admits or excludes evidence unless a substantial right of the party is affected, and
>
> (1) Objection. In case the ruling is one admitting evidence, a timely objection or motion to strike appears of record, stating the specific ground of objection, if the specific ground was not apparent from the context;

MISS. R. EVID. 103(a)(1).

[110] *See supra* note 40. The supreme court noted that Rule 103 is in accord with decisions of the court prior to the enactment of the Mississippi Rules of Evidence. *Peterson*, 518 So. 2d at 635; *see* Murphy v. State, 453 So. 2d 1290, 1293-94 (Miss. 1984) (where ground for objection is apparent from context, specific objection is not required).

[111] *Peterson*, 518 So. 2d at 635.

[112] *Id.* at 635-36. Rule 609(a)(1) provides:

> (a) General Rule. For the purpose of attacking the credibility of a witness, evidence that he has been convicted of a crime shall be admitted if elicited from him or established by public record during cross-examination but only if the crime (1) was punishable by death or imprisonment in excess of one year under the law under which he was convicted, and the court determines that the probative value of admitting this evidence outweighs its prejudicial effect on a party or (2) involved dishonesty or false statement, regardless of the punishment.

MISS. R. EVID. 609(a)(1).

[113] *Id.*

[114] *Peterson*, 518 So. 2d at 636.

[115] *Id.*; *see* United States v. Preston, 608 F.2d 626, 639 (5th Cir. 1979) (finding that probative value outweighs prejudicial effect must be made on record).

[116] *Peterson*, 518 So. 2d at 636.

IV. YOUTH COURT ACT

Only three cases were rendered by the Mississippi Supreme Court in 1987 relating to the Youth Court Act.[121] The primary case of importance is *Yarborough v. State*.[122] Robert W. Yarborough was tried for the rape of his fourteen-year-old daughter, K.Y.[123] At the trial, K.Y.

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[117] *Id.* Since this case was the first interpretation of Rule 609, the supreme court listed four general factors to consider in conducting this analysis: "(1) the kind of crime involved; (2) when the conviction occurred; (3) importance of the witness' testimony to the case; (4) the importance of the credibility of the defendant." *Id.*; *see* United States v. Preston, 608 F.2d 626, 639 n.14 (5th Cir. 1979) (setting forth factors to consider).

[118] *Peterson*, 518 So. 2d at 637-38; *see* Gordon v. United States, 383 F.2d 936, 940 (D.C. Cir. 1967) (outlining specific factors adopted by Mississippi Supreme Court); 3 J. WEINSTEIN, EVIDENCE ¶ 609[04], at 688-89 (1987) (same).

[119] *Peterson*, 518 So. 2d at 638. Defense counsel also argued that the trial court erred in failing to grant a limiting instruction, even though no such instruction was requested by defense counsel. *Id.* at 637-38. Following the Fifth Circuit rule in United States v. Diaz, 585 F.2d 116, 118 (5th Cir. 1978), the Mississippi Supreme Court stated that trial judges should grant a limiting instruction *sua sponte* when defense counsel fails to make a proper request. *Peterson*, 518 So. 2d at 638.

[120] *Peterson*, 518 So. 2d at 640. In addition to Rule 103 and Rule 609, the supreme court interpreted Rule 803(1), the present sense impression exception to the hearsay rule. *Id.* at 639-40. The court set forth three requirements for the exception to apply: "(1) A statement must be made while the event or condition is being perceived by the declarant or 'immediately thereafter'; (2) The declarant must 'perceive' the event or condition; (3) The statement must describe or explain the event or condition." *Id.* at 640; *see* 4 J. WEINSTEIN, EVIDENCE ¶ 803(1)[01], at 875-81 (1987) (describing three requirements for Rule 803(1)).

[121] *See* In the Interest of W.B., 515 So. 2d 1175, 1177 (Miss. 1987) (where minor is charged under Youth Court Act with receiving stolen property, guilty knowledge on part of accused must be both alleged and proved beyond reasonable doubt); Gardner v. State, 514 So. 2d 292, 294 (Miss. 1987) (1983 amendments to Youth Court Act do not govern punishment and sentencing considerations for crime committed before their enactment).

[122] 514 So. 2d 1215 (Miss. 1987).

[123] *Id.* The rape occurred at the home of Melvin St. Amant, who, along with his son

testified unequivocally to the circumstances under which she was raped by Yarborough.[124] The Circuit Court of Jackson County convicted Yarborough of rape and sentenced him to twenty years imprisonment.[125] Although he declined to appeal the conviction and sentence, Yarborough filed a pro se motion to vacate the conviction and sentence based upon the claim that K.Y. recanted her testimony.[126] The petition for post-conviction relief was denied by the circuit court.[127]

Appealing the holding of the lower court, Yarborough asserted two assignments of error.[128] First, Yarborough contended that the trial court erred in admitting K.Y.'s testimony taken in a youth court proceeding where she stated that her father had raped her.[129] Relying on section 43-21-261(1)(c) of the Mississippi Code,[130] Yarborough argued that the contents of the youth court records are confidential and should remain undisclosed unless ordered by the youth court pursuant to 43-21-261 of the Mississippi Code.[131] Since section 43-21-261(1)(c) permits disclosure to "a judge of any other court" only upon order of

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Justin, witnessed the rape. *Id.* at 1216. Yarborough denied the allegations, claiming he was at home asleep when the incident was said to have transpired. *Id.*

[124] *Id.* at 1215.

[125] *Yarborough*, 514 So. 2d at 1215.

[126] *Id.* K.Y. wrote two letters, one addressed to Yarborough's attorney and the other "To Whom It May Concern", wherein she recanted her previous testimony regarding the rape. *Id.* at 1216. Thereafter, a youth court proceeding was conducted where the letters were discussed. *Id.* At the proceeding, K.Y. reaffirmed her original testimony that Yarborough had raped her. *Id.*

[127] *Id.* The circuit court found that K.Y. retracted her testimony only because she desired reconciliation with her family, and it was only when K.Y. was among family members that she withdrew her testimony. *Id.*

[128] *Id.*

[129] *Id.*

[130] *Id.* at 1217. Section 43-21-251(2) provides: "The records of the youth courts and the contents thereof shall be kept confidential and shall not be disclosed except as provided in section 43-21-261." MISS. CODE ANN. § 43-21-251 (1972).

[131] *Yarborough*, 515 So. 2d at 1217. Section 43-21-261(1)(c) provides:

> (1) Except as otherwise provided in this section, records involving children shall not be disclosed, other than to necessary staff of the youth court, except pursuant to an order of the youth court specifying the person or persons to whom the records may be disclosed, the extent of the records which may be disclosed and the purpose of the disclosure. Such court orders for disclosure shall be limited to those instances in which the youth court concludes in its discretion that disclosure is required for the best interests of the child, the public safety or the functioning of the youth court and then only to the following persons:
>
> (c) A judge or any other court or member of another court staff;

MISS. CODE ANN. § 43-21-261(1)(c) (Supp. 1986).

the youth court,[132] and since no such order was obtained in the instant case, Yarborough argued that the statements made by K.Y. in the youth court proceeding should not have been allowed into evidence at the trial below.[133]

In addressing this issue, the Mississippi Supreme Court stated that although no order from the youth court was obtained to disclose K.Y.'s testimony to the court, prior approval of the youth court is not necessary when such records are used to impeach the testimony of a witness in a criminal proceeding.[134] The supreme court reasoned that because the confidentiality requirement is for the protection of the youth, the literal language of the statute should not shield an adult when the focus of the youth court testimony is to test the truth of the charges against the adult.[135] As such, the court rejected Yarborough's contention and held that section 43-21-261(1)(c) does not require the youth court to authorize the disclosure of impeachment testimony before it is used against a criminal defendant.[136]

In his second assignment of error, Yarborough contended that the lower court erred in failing to give credit to K.Y.'s proferred recantation.[137] However, the supreme court, noting the unreliability of recanted testimony,[138] concluded that the trial court was correct in finding that the recanted testimony was a product of influence by K.Y.'s family members.[139] Therefore, having found no error at the trial court, the Mississippi Supreme Court affirmed.[140]

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[132] *Id.*

[133] *Yarborough*, 514 So. 2d at 1217. Yarborough contended that to allow the testimony from the youth court proceeding into evidence would undermine the confidentiality of the youth court proceedings. *Id.*

[134] *Id.* at 1218. The court relied on Hamburg v. Sate, 248 So. 2d 430, 433-34 (Miss. 1971), which held that the knowledge of a juvenile delinquent could be turned over to proper officials where such information was not used against the juvenile. *Yarborough*, 514 So. 2d at 1218.

[135] *Yarborough*, 514 So. 2d at 1219. Although the court declined to reverse for want of form under these circumstances, it warned against any attitude of judicial laxity toward the confidentiality of the youth court proceedings. *Id.* at 1219 n.2.

[136] *Id.* at 1218.

[137] *Id.* at 1219.

[138] *Id.* at 1220. "No form of proof is so unreliable as recanting testimony." (citing People v. Van Der Dreissche, 206 N.W. 339, 341 (Mich. 1925)).

[139] *Yarborough*, 514 So. 2d at 1220. Since the findings of the trial court sitting without a jury were supported by substantial credible evidence, the supreme court upheld the lower court's ruling. *Id.*

[140] *Id.* at 1221.

V. PERJURY

"Every person who shall wilfully and corruptly swear, testify or affirm falsely to any material matter under oath, affirmation or declaration legally administered in any matter, cause or proceeding pending in any court of law or equity, or before any office thereof, . . . shall be convicted of perjury . . . ."[141] In *Hogan v. State*,[142] the Mississippi Supreme Court reviewed the validity of a perjury conviction.[143] Pursuant to a plea bargaining agreement, Otha D. Hogan, Jr. plead guilty to manslaughter in the Circuit Court of Lamar County on October 14, 1982.[144] Hogan stated under oath before the court that he freely and voluntarily entered the plea and fully understood the consequences thereof.[145] Then, on February 27, 1984, Hogan filed a petition for a writ of habeas corpus under oath, asserting that he did not understand the plea and that such plea was involuntary and not willfully given.[146] Hogan was subsequently tried and found guilty of perjury.[147]

Appealing the conviction, Hogan argued that the prosecution failed to prove which statement made by Hogan under oath was false.[148] The question before the Mississippi Supreme Court was "whether proof that an accused knowingly and wilfully has made two mutually contradictory statements on a material matter under oath without more can support a conviction of perjury under this statute."[149] In an ordinary case, the State is required to produce two witnesses or one witness plus corroborating evidence that the accused committed perjury.[150] The State is in a position to demonstrate on which date the defendant lied and can prove the perjury by introducing the true facts as to that date by providing independent evidence, or evidence aliunde.[151] However, in special situations such as the instant case, the State should not be required to independently corroborate the mutually contradictory statements when, as a practical matter, the defendant could not have been mistaken and is the only person in a position to know which statement was true.[152] Thus, the supreme court concluded that where a defendant has been charged with perjury on the basis of two contradictory sworn statements, and there is no independent evidence available to the State as to which of the statements is true, then the State may proceed to trial solely on the contradictory statements.[153] The court cautioned, however, that where there is evidence indicating on which date the accused lied, the State must prove such evidence.[154] In the instant case, since it appeared from the record that such evidence was available to the State, the supreme court reversed and remanded.[155]

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[141] MISS. CODE ANN. § 97-9-59 (1972).

[142] 516 So. 2d 474 (Miss. 1987).

[143] *See also* McFee v. State, 510 So. 2d 790, 793 (Miss. 1987) (where accused has made conflicting sworn statements, one witness testifying to falsity of statement with which he is charged is sufficient to sustain conviction for perjury).

[144] *Hogan*, 516 So. 2d at 475. Hogan had been indicted by the grand jury of Lamar County on a charge of murder. *Id.* However, he plead guilty to the reduced charge of manslaughter on the day the case had been set for trial. *Id.*

[145] *Id.*

[146] *Id.*

[147] *Id.* at 477.

[148] *Id.* Hogan also moved to quash the indictment, claiming that it failed to allege "every essential element" of the crime. *Id.* at 476.

[149] *Id.* at 477.

[150] *Hogan*, 515 So. 2d at 477. In such cases, the contradictory statements are strong corroborating evidence of the perjury. *Id.*

Justice Robertson, joined by Chief Justice Roy Noble Lee and Justice Prather, concurred with the majority that Hogan's conviction was properly reversed.[156] However, Justice Robertson argued that the State should not be relieved of alleging and proving, by evidence aliunde, which statement was false and which was true with respect to the matter involved.[157] Although recognizing the problems of proof presented by the case, Justice Robertson nevertheless thought that the majority erred in relieving the State of part of its burden where evidence aliunde was unavailable.[158] Therefore, Justice Robertson argued that the case should have been rendered, not remanded.[159]

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[151] *Id.* at 479.

[152] *Id.* at 481. If the State was not allowed to proceed on a perjury charge where only the accused has knowledge of which statement was false, manifest unjustice would result against society. *Id.*

[153] *Id.* In so holding, the Mississippi Supreme Court departed from the general rule as well as from the rule in Mississippi requiring proof of the false statement. *Id.* at 482. Since the rule was not a product of the applicable statute, but of common law only, the supreme court chose to adopt a more rational and equitable rule. *Hogan*, 515 So. 2d at 482.

[154] *Hogan*, 515 So. 2d at 481-82. It is only where there is no independent evidence that the State is allowed to proceed solely on the contradictory statements. *Id.*

[155] *Id.* at 483.

[156] *Id.*

[157] *Id.* at 484-85. "A common sense reading of this statute requires that the prosecution allege and prove the occasion on which the false statement was made." *Id.* at 483.

[158] *Id.* at 484.

[159] *Id.* at 485.

VI. CONTEMPT OF COURT

Criminal contempt of court, an offense against the court as a legal institution and not against the individual judge, was the focus of *Culpepper v. State*.[160] Charles L. Culpepper appeared before the Chancery Court of Lowndes County as the attorney for Thomas C. Harvey in a domestic relations dispute.[161] Each Lowndes County chancery judge withdrew from the cause, and Chancery Judge Nathan P. Adams, Jr. of Washington County heard the cause as a special judge.[162] The physical location of the hearing was the Washington County Chancery Court.[163]

Culpepper subsequently misrepresented to the court matters regarding settlement negotiations.[164] As a result, Culpepper was charged with and found guilty of constructive contempt of court by the Chancery Court of Washington County.[165] Appealing the conviction, Culpepper argued that the Chancery Court of Washington County lacked jurisdiction to hear the contempt charge.[166]

Relying on section 11-1-11 of the Mississippi Code,[167] the Mississippi Supreme Court concluded that the contempt occurred against the Chancery Court of Lowndes County, not Washington County.[168] Even though the geographical location of the domestic hearing was Washington County, Lowndes County retained jurisdiction over the contempt matter since the Washington County special judge merely sat in the place of the recused Lowndes County chancellors.[169] Since only the offended court has jurisdiction to punish the contemnor, the supreme court reversed and rendered.[170]

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[160] 516 So. 2d 485 (Miss. 1987); *see also* Varvaris v. State, 512 So. 2d 886, 888-89 (Miss. 1987) (where defendant is charged with direct criminal contempt, since contempt is committed in presence of court, offended judge may rule on contempt).

[161] *Culpepper*, 516 So. 2d at 486. The dispute concerned an alleged violation of child custody provisions which were enacted pursuant to a divorce decree. *Id.*

[162] *Id.*

[163] *Id.*

[164] *Id.* The false representation made by Culpepper to the court was that his client was ready to settle the case. In actuality, however, his client had no knowledge whatsoever of the proposed settlement. *Id.*

[165] *Id.* Culpepper was fined $500.00 and sentenced to a thirty-day suspended jail term. *Id.*

[166] *Id.*

[167] *Id.* at 486. Section 11-1-11 provides:

> When the circuit judge, county judge or chancellor, by reason of interest or other cause, shall be disqualified to sit in any case, the parties may select some other member of the bar; and thereupon the judge or chancellor shall retire from the bench for the time, and the [special judge or chancellor] shall take his place and hear and determine the cause. The proceedings shall be entered if the same were had before the judge or chancellor . . . .

MISS. CODE ANN. § 11-1-11 (1972).

[168] *Culpepper*, 516 So. 2d at 486-87.

The Mississippi Supreme Court in 1987 rendered cases in the areas of indictments,[171] plea bargains,[172] and search and seizure[173] which were not discussed textually. Other miscellaneous cases which are not susceptible to individual categorization were also decided.[174]

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[169] *Id.* at 487. Criminal contempt of court is considered an offense against the court as a legal institution and not against the judge as an individual. *Id.* at 486.

[170] *Id.* at 488; *see* Prine v. State, 108 So. 716 (Miss. 1926) (punishment for criminal contempt rests exclusively with court against whom contempt was directed).

[171] Cases relating to indictments include the following: Hooker v. State, 516 So. 2d 1349, 1351-52 (Miss. 1987)(where indictment is brought within statute of limitations period, defendant must show actual prejudice and intentional governmental delay for due process rights to be violated); Cummins v. State, 515 So. 2d 869, 872 (Miss. 1987) (indictment which tracks language of applicable statute is sufficient); Hentz v. State, 510 So. 2d 515, 516 (Miss. 1987) (indictment for subordination of perjury must state circumstances of issue or point of inquiry in which perjury was committed); State v. Rivenbark, 509 So. 2d 1047, 1048-49 (Miss. 1987)(where events listed in indictment for false pretenses fail to support conclusion that property or money was actually obtained to detriment of party deceived, indictment fails to allege crime under Mississippi law); State v. Hoffman, 508 So. 2d 669, 671 (Miss. 1987) (where criminal information formally charging defendant with commission of crime fails to contain plain, concise, and definite statement of facts which constitute offense charged and fails to adequately appraise defendant of nature of charge against him, dismissal of charge is proper); Shive v. State, 507 So. 2d 898, 900 (Miss. 1987) (indictment may be properly amended only for matters of form, not substance); State v. Lott, 507 So. 2d 378, 379-80 (Miss. 1987) (indictment for false pretenses that fails to allege that property was received to detriment or injury of person from whom it was obtained fails to allege facts constituting crime); Reed v. State, 506 So. 2d 277, 279-80 (Miss. 1987) (where a trial judge permits indictment alleging armed robbery of three victims to be amended at trial, removing name of one of victims from indictment after state neglected to obtain that victim as witness, and fails to enter order in record authorizing amendment, indictment as to that victim will be dismissed with prejudice); State v. Allen, 505 So. 2d 1024, 1025 (Miss. 1987) (indictment for false pretenses that fails to charge false representation of past or present fact does not properly charge crime under positive Mississippi law); Armstead v. State, 503 So. 2d 281, 283 (Miss. 1987) (although indictment charging defendant with attempted rape does not include term "intent", defendant is sufficiently notified of nature and cause of accusation against him if indictment charges him with "willfully and feloniously" attempting rape).

[172] *See* Pierce v. State, 507 So. 2d 372, 375 (Miss. 1987) (state may not enter plea bargain agreement with defendant and then claim "no bargain" when defendant fails to raise settlement amount); Hentz v. State, 503 So. 2d 262, 264-65 (Miss. 1987) (lower court did not err in dismissing motion to set aside guilty plea).

[173] *See* Smith v. State, 505 So. 2d 1194, 1196 (Miss. 1987) (where previously reliable confidential informant provides information concerning narcotic activity, substantial basis exists for determining probable cause to issue search warrant); Fleming v. State, 502 So. 2d 327, 329 (Miss. 1987) (once probable cause exists, officers are justified in conducting as thorough search as magistrate could authorize by warrant).

VII. Ineffective Assistance of Counsel

The Mississippi Supreme Court decided several cases addressing the issue of a defendant's right to effective counsel.[175] While it is not uncommon for cases of this sort to be decided solely in light of the two-pronged test of *Strickland v. Washington*,[176] the Mississippi Supreme Court held in *Ferguson v. State*,[177] that while an attorney's actions may not amount to ineffectiveness under the *Strickland* test, they may cause a trial to be inherently unfair, and consequently require reversal. In *Ferguson*, a bench trial, defendant's trial counsel, among other things, told the trier of fact that his client was a liar.[178] Applying the *Strickland* test, the court held that although the attorney's actions were deficient, counsel was not ineffective because the evidence strongly suggested that the defendant was guilty.[179] However, the court observed that a finding of *effective* assistance by counsel does not end the inquiry because the sixth amendment "has many mansions,"[180] in particular, the right to a fair trial.[181] Consequently, although both parties focused solely on the issue of effective assistance of counsel, the court reversed and remanded, holding that a case in which counsel denounced his client as a liar in front of the trier of fact constituted an independent violation[182] of the sixth amendment, was inherently unfair, and required reversal.

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[174] Miscellaneous cases include the following: Faraga v. State, 514 So. 2d 295, 306 (Miss. 1987) (where defendant is convicted of capital murder and underlying felony is felony child abuse, one act of abuse will be sufficient to support conviction); Williams v. State, 512 So. 2d 666, 669 (Miss. 1987) (when defendant is convicted of burglary in addition to breaking and entering, crime need not be proved, only intent to commit some crime while in dwelling); Buckley v. State, 511 So. 2d 1354, 1357 (Miss. 1987) (where defendant admits to prior criminal conviction on cross examination, prior reference made to his "rap sheet" by witness for prosecution is not prejudicial to defendant); Booker v. State, 511 So. 2d 1329, 1332 (Miss. 1987) (where prosecutor's statements to jury alluding to appellate review of death penalty are responsive to, or invited by statements previously made by defense counsel, any error that occurred is considered "invited error" and sentence of death arising out of those circumstances will be affirmed); Burk v. State, 506 So. 2d 993, 993 (Miss. 1987) (M'Naughten rule remains legal definition of insanity in Mississippi); Cantrell v. State, 507 So. 2d 325, 327-28 (Miss. 1987) (judge is not disqualified from sitting at trial merely because of previous participation in other legal proceedings against defendant); Meshell v. State, 506 So. 2d 989, 992 (Miss. 1987) (where blow to victim's head by defendant was actual cause of victim's death, transportation away from treating hospital by victim's family against advice of attending physicians does not constitute intervening cause absolving defendant from responsibility for victim's death); Howard v. State, 507 So. 2d 58, 62 (Miss. 1987) (where tape-recorded conversation is irrelevant to defense of entrapment and too remote from date of incident, it will be excluded); Gibson v. State, 503 So. 2d 230, 233-34 (Miss. 1987) (where defendant exhibited signs of intoxication immediately following his involvement in fatal accident, officer had probable cause to take blood sample absent arrest); Roberson v. State, 501 So. 2d 398, 401 (Miss. 1987) (only intent necessary to complete act of sexual battery is intent to do act); Martin v. State, 501 So. 2d 1124, 1127-28 (Miss. 1987) (with respect to muscadine and other native Mississippi wines, provisions of Miss. Code Ann. §§ 67-5-1, et seq., also known as Mississippi Native Wine Law of 1976, supercede general statutes regarding alcoholic beverages contained in Chapters One and Three, Title 67, of Mississippi Code).

[175] Harrison v. State, 520 So. 2d 1352, 1353 (Miss. 1987)(motion to substitute counsel within discretion of trial judge); Wright v. State, 512 So. 2d 679, 681 (Miss. 1987)(absent showing of direct harm, no error in delay of affording defendant counsel); Ferguson v. State, 507 So. 2d 94, 97 (Miss. 1987)(although actions may not constitute ineffectiveness under *Strickland* test, they may cause trial to be inherently unfair in violation of sixth amendment); Waldrop v. State, 506 So. 2d 275, 275 (Miss. 1987)(to prove ineffective assistance of counsel, defendant must meet *Strickland* test); King v. State, 503 So. 2d 271, 273 (Miss. 1987)(same); Alexander v. State, 503 So. 2d 235, 240 (Miss. 1987)(same); Knox v. State, 502 So. 2d 672, 676 (Miss. 1987)(same).

[176] 466 U.S. 668 (1984). Mississippi adopted the two-pronged test announced in

Harrison v. State[183] concerned a defendant who was denied his request to have the attorney of his choice appear for him. In *Harrison*, the defendant was appointed counsel following an indigency hearing. However, on the day of his trial, a second attorney who had been retained by the defendant appeared and requested a continuance. The trial court conditioned substitution of counsel on the repayment by the defendant of expenses incurred in preparation for the trial to the county. When Harrison replied that he did not have the money, the trial court denied his motion for substitution of counsel and proceeded to trial.[184] Further, the trial court noted that had Harrison desired to

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Strickland in Gilliad v. State, 462 So. 2d 710 (Miss. 1985). Under *Strickland*, for a defendant to prove he had ineffective assistance of counsel, he must prove, (1) counsel's performance was deficient, and (2) this deficiency was prejudicial to the defendant. *Strickland*, 466 U.S. at 689.

[177] 507 So. 2d 94 (Miss. 1987).

[178] *Id.* at 96. Defendant's trial counsel also failed to meet with him prior to trial to discuss details of the allegations, was deficient in pretrial investigations, and failed to make an independent investigation of the facts of the case. *Id.* at 96-97.

[179] *Id.* at 95.

[180] *Id.* at 96.

[181] *Id.* The court noted that although only the question of ineffective assistance of counsel was addressed in the appeal briefs, the court may, under Miss. S. Ct. R. 6(b), examine other constitutional violations which may exist. *Id.*

[182] *Id.* at 97. That is, independent from the sixth amendment violation of the right to effective counsel.

[183] 520 So. 2d 1352 (Miss. 1987).

[184] *Id.* at 1353. Trial preparation expenses incurred by Jones County were $500.00. *Id.*

retain counsel of his own choosing he had ample time before the trial in which to do so.[185] Harrison appealed his conviction,[186] arguing that he had an absolute right to retain counsel of his choice.[187] However, the Mississippi Supreme Court held that Harrison's request for substitution of counsel was untimely; consequently, action on the request lay within the sound discretion of the trial court.[188]

In his concurrence, Justice Robertson[189] focused on Jones County's apparent policy of requiring defendants in Harrison's position to pay incurred expenses before being allowed to substitute counsel of choice. Justice Robertson unequivocally stated that there is no authority for such a policy, and consequently it may not be used to deny a defendant his choice of counsel.[190] Robertson further noted that had the new counsel been ready to proceed with the trial, there would have been no authority to deny the counsel substitution.[191]

VIII. POST-CONVICTION RELIEF

Several cases were presented to the court addressing the issue of post-conviction relief.[192] The Mississippi Uniform Post-Conviction Relief Act[193] affords prisoners a procedure by which claims are reviewed which could not have, in practicality, been raised at trial or on direct appeal.[194] Consequently, if the prisoner could have, but failed to, raise the claims at the trial or on direct appeal, these are forever waived *unless* there is a showing of cause or of actual prejudice to the prisoner necessitating relief from the waiver.[195] In addition, in order for a petition for post-conviction relief to be granted, there must be a showing of a denial of a state or federal right.[196] The most common claims in an application for post-conviction relief are ineffective assistance of counsel and denial of the right to take the stand in one's own defense.[197]

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[185] *Id.*

[186] Harrison was convicted for the sale of cocaine. *Id.* at 1352.

[187] *See* Powell v. Alabama, 287 U.S. 45 (1932)(defendant entitled to secure counsel of choice); *see also* MISS. CONST. art. III, § 26 (giving defendants in Mississippi the right to secure counsel of choice).

[188] *Harrison*, 520 So. 2d at 1354. *See* Collins v. State, 369 So. 2d 500 (Miss. 1979)(where indigent defendant appears on trial day with new lawyer requesting continuance, such grant within court's discretion).

[189] Joined by Justices Hawkins, Prather, Lee, Sullivan, Anderson and Zuccaro. *Harrison* 520 So. 2d at 1354.

[190] *Id.* at 1355 (Robertson, J., concurring).

[191] *Id.*

[192] Those not textually discussed are as follows: Wiley v. State, 517 So. 2d 1373, 1379 (Miss. 1987)(post-conviction relief petition alleging ineffective assistance of counsel must meet *Strickland* test); Merritt v. State, 517 So. 2d 517, 518-20 (Miss. 1987)(same); Jimpson v. State, 511 So. 2d 501, 501 (Miss. 1987)(where case record insufficient for court to examine post-conviction relief motion on merits, case will be remanded); Johnson v. State, 508 So. 2d 1126, 1128-29 (Miss. 1987)(assignment of error raised for first time in post-conviction relief petition procedurally barred absent sufficient cause); Jackson v. State, 506 So. 2d 994, 995 (Miss. 1987)(three-year limitation of Post-Conviction Collateral Relief Act operates prospectively); Tobias v. State, 505 So. 2d 1014, 1015 (Miss. 1987)(where state's witness commits perjury and so admits in affidavit, defendant is entitled to evidentiary hearing).

[193] MISS. CODE ANN. § 99-39-1 to -29 (Supp. 1986).

In *Neal v. State*,[198] the defendant had applied for post-conviction relief alleging both of the above-stated claims. The Mississippi Supreme Court did allow an evidentiary hearing based upon the allegation of denial of the right to take the stand, but before so doing, spelled out the procedure and purpose of post-conviction relief.[199] The court stated that the "procedural posture is analogous to that when a defendant in a civil action moves to dismiss for failure to state a claim"[200] and that the function of section 99-39-9 of the Mississippi Code is the same as that of Rules 8(a) and (3) of the Mississippi Rules of Civil Procedure[201] Further, the court stated that a defendant is required to give a "substantial and detailed threshold showing"[202] far above that required in comparable civil actions,[203] and that this is accomplished by following the components of section 99-39-9, namely, giving sworn pleadings of facts within the prisoner's personal knowledge, and affidavits by witnesses of facts not within the prisoner's personal knowledge.[204]

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[194] *See* MISS. CODE ANN. 99-39-3 (Supp. 1986)(describing purpose of Post-Conviction Relief Act). MISS. CODE ANN. § 99-39-21(1) (Supp. 1986) states:

> Failure by a prisoner to raise objections, defenses, claims, questions, issues or errors either in fact or law which were capable of determination at trial and/or on direct appeal . . . shall constitute a waiver thereof and shall be procedurally barred, but the court may upon a showing *of cause* and *actual prejudice* grant relief from the waiver. (emphasis added) .

[195] MISS. CODE ANN. § 99-39-21(4) (Supp. 1986) defines cause as being limited to those cases "where the legal foundation . . . could not have been discovered . . . at the time of trial or direct appeal." MISS. CODE ANN. § 99-39-21(5) (Supp. 1986) defines actual prejudice as being limited to those errors "which would have actually adversely affected the ultimate outcome."

[196] *See* MISS. CODE ANN. § 99-39-27(5) (Supp. 1986)(announcing requirement of violation of state or federal right for relief petitions.

[197] *See* Johnson v. State, 511 So. 2d 1333, 1333 (Miss. 1987)(listing complaints commonly found in relief petitions).

[198] 525 So. 2d 1279 (Miss. 1987).

[199] *Id.* at 1280-81.

[200] *Id.* at 1280.

[201] *Id.*

[202] *Id.*

[203] *Id.* This is so because there has been a valid final judgment handed down, and the court consequently requires a strong showing from the defendant requesting relief. *Id.*

Billiot v. State[205] followed in the footsteps of *Neal* and the court again stated that where a defendant applies for post-conviction relief, he must follow the guidelines of section 99-39-9.[206] Billiot had alleged in his application that he was presently insane and accordingly, was exempted under provisions of the United States Constitution[207] from being executed.[208] The court found that Billiot had met the statutory requirements and consequently, granted an evidentiary hearing.[209] The court then looked at the state statute and federal case law dealing with the pleading of insanity in a post-conviction relief application.[210] Where insanity is plead in a post-conviction petition, Mississippi's statute requires that the insanity have occurred *after* the defendant's conviction.[211] This intervening aspect, however, is not a requirement in federal case law.[212] Accordingly, holding that state law must yield to federal law when a conflict exists, the court observed that the viability of Mississippi's intervention requirement may be close to an end.[213]

An interesting proposition was presented to the court in the case of *Johnson v. State*.[214] Here, Johnson had been sentenced to death by a Mississippi jury. The jury used three aggravating circumstances to support this verdict, one being a prior New York conviction of second degree assault and first degree intent to commit rape.[215] Following the Mississippi conviction, Johnson successfully petitioned to have the New York conviction reversed and vacated.[216] Consequently, Johnson argued that this should not be allowed to be considered by the jury in the sentencing phase.[217] The Mississippi Supreme Court rejected this reasoning, noting that it is not uncommon for foreign states to overturn prior convictions through collateral attack,[218] and further, that a prior conviction is a useful guideline for a jury in cases such as this.[219] Specifically, the court refused to allow conviction reversals in foreign states to have the effect of lessening the effect of death penalty verdicts in this state.[220]

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[204] *Id.* at 1280-81. MISS. CODE ANN. § 99-39-9 (Supp. 1986).

[205] 515 So. 2d 1234 (Miss. 1987).

[206] *See supra* note 28 and accompanying text.

[207] *See* Ford v. Wainwright, 477 U.S. 399 (1986)(unconstitutional under eighth amendment to execute one who is presently insane). *See also* U.S. CONST. amend. VIII (prohibiting cruel and inhumane treatment).

[208] *Billiot*, 515 So. 2d at 1235.

[209] *Id.* at 1238.

[210] *Id.* at 1236. MISS. CODE ANN. § 99-19-57(2)(a) (Supp. 1986) provides, in part "If it is believed that a convict . . . has become insane *since the judgment of the court*, the following shall be the exclusive [procedure available]." (emphasis added).

[211] *Id.*

[212] *Billiot*, 515 So. 2d at 1236.

[213] *Id.*

[214] 511 So. 2d 1333 (Miss. 1987).

[215] *Johnson*, 511 So. 2d at 1336.

[216] *Id.* at 1337.

IX. Cross-Examination

In general, the cases before the court in 1987 dealing with the issues pertaining to cross-examination[221] were decided by application of well-established principles of the art of cross-examination and the rules of evidence.

One of these well-established rules of evidence is that a defendant has the right to take the stand in his own trial;[222] however, if he fails to do so, this failure *may not* be commented upon.[223] A new dimension to this proposition was presented in *Monroe v. State.*[224] In *Monroe*, the prosecuting attorney cross-examined Jethro Jones, one of the defendant's witnesses, who had previously been convicted of robbery in connection with the same incident on which Monroe was presently being tried.[225] During cross-examination, the prosecution was able to make Jones admit that he had failed to take the stand at his own trial.[226]

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[217] *Id.* Defendant reasoned that since the conviction was no longer valid, the jury couldn't reasonably use that as an aggravating circumstance against him. *Id.*

[218] *Id.* at 1338. The court noted, however, that even had this circumstance not been considered by the jury, the remaining two aggravating circumstances considered would have been strong enough to support the verdict. *Id.* at 1337.

[219] *Id.* at 1338.

[220] *Id.* The court did, however, decline to rule on whether cases which are overturned on *direct appeal* may be considered to be an aggravating circumstance, and pointed out that this conviction had been turned over on *collateral attack. Id.*

[221] Those cases not reported textually are Hill v. State, 512 So. 2d 883, 887-88 (Miss. 1987)(witnesses may be cross-examined regarding possible promises of leniency); Foster v. State, 508 So. 2d 111, 1104 (Miss. 1987)(same); Black v. State, 506 So. 2d 264, 267 (Miss. 1987)(judge may deny cross examination on legally irrelevant material).

[222] *See* Culberson v. State, 412 So. 2d 1184, 1186 (Miss. 1982)(holding that defendant has constitutional right to take stand in his own behalf).

[223] *See* Miss. Code Ann. § 13-1-9 (Supp. 1986)(prohibiting comment during trial on defendant's failure to take stand). It does not matter if the comment is positive or negative. Yarbrough v. State, 70 Miss. 593, 12 So. 551 (1893). Likewise, insinuations and innuendos are forbidden. Wilson v. State, 443 So. 2d 1142 (Miss. 1983).

[224] 515 So. 2d 860 (Miss. 1987).

[225] *Monroe*, 515 So. 2d at 864.

[226] *Id.* No contemporaneous objection was made by the defense counsel during this

There were, however, no questions asked of Jones directly referring to Monroe's right to take the stand.[227] On appeal, the Mississippi Supreme Court looked at this issue of whether questioning a witness about his own failure to take the stand in his previous trial, but not questioning the witness about the *defendant's* failure to take the stand, amounted to a "comment" by the attorney.[228] The court found this not to be a comment on Monroe's failure to testify because it was not a direct comment or an insinuation concerning Monroe's right to testify, but instead referred solely to Jones' trial tactics.[229]

Suan v. State[230] dealt with a defendant's right to impeach a witness by showing bias. During the trial, the defense attorney attempted to cross examine Eddie Grammer, the prosecution's witness, who had identified Suan as the person whom he had witnessed aid in the escape of a fellow prisoner from a county work center.[231] The defense counsel wished to question Grammer about the fact that he had been in trouble with authorities but had not been prosecuted.[232] This was an attempt to imply that Grammer had been given lenient treatment in return for his testimony against the defendant,[233] and consequently, that Grammer had a motive to falsely testify. This line of questioning, however, was quashed through sustained objections.[234] On appeal, the court found this to be reversible error, holding that a defendant has a right to broad and extensive cross-examination.[235] The court concluded that a defendant has a definite interest in cross-examining a witness who may have been promised leniency and freedom from prosecution in return for providing state's testimony, implying that the witness'

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line of questioning, procedurally barring this argument of this assignment of error on appeal. *Id.* The court, however, chose to address this issue stating that commenting upon a defendant's failure to take the stand violates "long established legal principles." *Id.*

[227] *Id.* at 865-66. The court noted that, for Monroe to win, there would have to be a finding that comments were made concerning *his* failure to testify. *Id.* at 865.

[228] *Id.* at 864-66.

[229] *Id.* at 866.

[230] 511 So. 2d 144 (Miss. 1987).

[231] *Suan*, 511 So. 2d at 145. Eddie Grammer had been incarcerated at the Simpson County Community Work Center along with Louis Mitchell Haynes, the convict that Suan allegedly helped escape. *Id.* Grammer testified that he witnessed Suan drive to the work center and pick up Haynes. *Id.*

[232] *Id.* at 147. Defense counsel attempted to question Grammer about some property he had allegedly stolen during a house burglary, but for which he was never prosecuted. *Id.*

[233] *Id.*

[234] *Id.*

[235] *Id.* at 147-48.

sole ambition was to testify in a manner pleasing to the prosecution.[236]

X. COMPETENCY

There were only two cases handed down in 1987 pertaining to the issue of competency.[237] The only case of consequence was *Griffin v. State*.[238] In *Griffin*, the defendant had been sentenced to life imprisonment.[239] At trial, the jury had been instructed that the State was required to prove only by a preponderance of the evidence that the defendant was competent to stand trial.[240] Griffin argued, however, that this instruction was erroneous and that the burden of proof standard should have been clear and convincing evidence.[241] The court, noting that the defendant was barred from asserting this argument because it was not properly preserved in accordance with Rule 42 of the Mississippi Supreme Court,[242] nevertheless stated that since the burden of proof standard at the federal level on competency issues is by a preponderance, then it was not plausible to require a heavier burden at the state level.[243]

XI. APPEAL

There were several cases handed down in 1987 dealing with the specifics of appellate procedure.[244] Two of these cases will be discussed textually, one discussing new trends in fingerprint identification, and the other clarifying existing discovery rules in criminal cases.[245] In *Giles v. State*,[246] the court dealt with the issue of whether or not an expert may identify fingerprints as being those of the defendant. In *Giles*, the defendant, who was convicted of bank robbery,[247] had been tracked down in California by the use of fingerprints which had been recovered from the crime scene.[248] During the trial, the prosecuting attorney asked a fingerprint expert[249] if the fingerprints recovered from the crime scene were the defendant's, and also if he believed that the defendant had touched a petty cash slip recovered from the crime scene.[250] On appeal, the defendant argued that it was error for a fingerprint expert to testify to an ultimate question of fact; namely, whether or not it was the defendant's fingerprints found at the scene.[251] In analyzing this issue, the Supreme Court focused on the modern trend of allowing an expert witness to identify fingerprints as being those of the defendant,[252] but failed to specifically state that Mississippi would fol-

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[236] *Id.* at 148.

[237] The two cases are Gammage v. State, 510 So. 2d 802 (Miss. 1987) and Griffin v. State, 504 So. 2d 186 (Miss. 1987).

[238] The other case, Gammage v. State, 510 So. 2d 802 (Miss. 1987), reiterated the holding in Dusky v. U.S., 362 U.S. 402 (1960), that a defendant is incompetent to stand trial when he cannot consult with his attorney using rational and factual understanding.

[239] *Griffin*, 504 So. 2d at 187.

[240] *Id.* at 190.

[241] *Id.* at 191.

[242] *Id.*

[243] *Id.* at 192.

[244] Jones v. State, 517 So. 2d 1295, 1300 (Miss. 1987)(not error to allow jury to consider multiple aggravating circumstances); Johnson v. State, 512 So. 2d 1246, 1250 (Miss. 1987)(circuit court does not lose jurisdiction over juveniles if charged with murder but convicted of offense which would have originally been in youth court's jurisdiction); Hughey v. State, 512 So. 2d 4, 8 (Miss. 1987)(33 month delay prior to trial not *per se* denial of right to speedy trial); Hickson v. State, 512 So. 2d 1, 3-4 (Miss. 1987)(hostile witnesses may be asked leading questions); Turner v. State, 505 So. 2d 284, 284 (Miss. 1987)(where appeal raises no issues requiring discussion, appeal raises no issues requiring discussion, conviction will be affirmed); Hill v. State, 505 So. 2d 281, 281 (Miss. 1987)(where appeal raises no issues requiring discussion, assignments will be affirmed); Jones v. State, 504 So. 2d 1196, 1198-1200 (Miss. 1987)(pretrial identification not im-

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proper unless impermissibly suggestive); Holliday v. State, 504 So. 2d 725, 726 (Miss. 1987)(when conviction for murder is not contrary to weight of evidence, it will not be overturned on appeal); Stever v. State, 503 So. 2d 227, 230 (Miss. 1987)(motion for directed verdict should be granted where evidence insufficient to support verdict); Carbins v. State, 502 So. 2d 659, 659 (Miss. 1987)(where appeal raises no issues requiring discussion, conviction will be affirmed); Triggs v. State, 502 So. 2d 626, 626 (Miss. 1987)(same); Brown v. State, 501 So. 2d 1131, 1132 (Miss. 1987)(directed verdict on issue of insanity will be affirmed in absence of proof of M'Naughten insanity); Peoples v. State, 501 So. 2d 424, 428-29 (Miss. 1987)(existence of and defendant's membership in conspiracy may be proved entirely by circumstantial evidence); Watkins v. State, 500 So. 2d 462, 463 (Miss. 1987)(in armed robbery case, trial judge cannot impose life sentence without jury recommendation).

[245] These two cases are Giles v. State, discussing modern trends in fingerprint identification testing, and Turner v. State, clarifying MISS. UNIF. R. OF CIR. CT. PRAC. 4.06.

[246] 501 So. 2d 406 (Miss. 1987).

[247] *Id.* at 407. The defendant was convicted of robbing the Clarksdale branch of Depositor's Federal Saving. *Id.*

[248] *Id.* Law enforcement officials took fingerprints off a door handle and cash receipts left at the crime scene. *Id.* These fingerprints led officials to the defendant in Bakersfield, California. *Id.* The defendant initially had an alibi that he was in California at the time of the robbery, but he failed to produce witnesses at trial testifying to that effect. *Id.*

[249] *Id.* The expert was Ron Smith of the Mississippi Crime Lab. *Id.* He compared the fingerprints obtained at the scene with those of an FBI fingerprint card on the defendant and testified that they matched, and further, that it was his opinion that the defendant's fingerprints were at the scene of the crime. *Id.* at 407-08.

[250] *Id. See supra* note 4.

[251] *Giles*, 501 So. 2d at 406-07.

[252] *Id.* at 408. The modern trend, however, is to allow nothing more than a statement that specific fingerprints are those of the defendant. *Id.* The expert generally is not

low in this trend. The court did state that the questioning of the expert had been overly conclusive,[253] but that, in light of other overwhelming evidence establishing the fingerprints as those of the defendant, no reversible error occurred.[254] It would be helpful to legal scholars and practitioners if the court would clarify in a future case whether or not this trend is to be followed in Mississippi.

In *Turner v. State*,[255] the court clarified the rule of discovery dealing with the disclosure by prosecution of an informant's name upon the request of the defendant. In this case, the defendant had filed a pretrial request for discovery in accordance with Rule 4.06 of the Mississippi Uniform Rules of Circuit Court Practice.[256] This request was not complied with and consequently, the defendant did not learn the name of the informant until during trial, some eighteen months later,[257] at which time he requested a continuance in order to locate and question the informant.[258] The trial judge, being informed by the prosecuting attorney that the informant's whereabouts were unknown, saw no possible benefit from a continuance and denied the request.[259] The court held this to be reversible error in this context because, under Rule 4.06, the defendant was entitled to be given the informant's name *upon request*, and failing this, a mid-trial continuance in order to give a defendant a reasonable opportunity to locate and question the witness.[260] Accordingly, prosecutors and trial judges alike should be aware that under similar circumstances, failure to comply with a Rule 4.06 request will constitute reversible error.

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allowed to conclude that the fingerprints at the scene of the crime are the defendant's. *Id.*

[253] *Id.*

[254] *Id.*

[255] 501 So. 2d 350 (Miss. 1987).

[256] *Id.* at 351. The rule states, in part:

> *Informants.* Disclosure of an informant's identify shall not be required *unless* the confidential information is to be produced at a hearing or trail or a failure to disclose his identity will infringe the constitutional right of the accused. Or *unless the informant depicts himself as eyewitness to the event . . .* constituting the charge against the defendant.

Miss. Unif. R. of Cir. Ct. Prac. 406(b)(2) (emphasis added).

[257] *Turner*, 501 So. 2d at 352. The informant was Cathy Johnson, who had witnessed part of the drug transaction for which Turner was being tried. *Id.* at 351-52. The prosecution lost contact with Johnson prior to trial and consequently, did not use her testimony at trial. *Id.* at 352.

[258] *Id.*

[259] *Id.*

[260] *Id.* at 352-53.

XII. MISCELLANEOUS

Several case decided on various miscellaneous issues were presented to the Mississippi Supreme Court in 1987.[261] The case of *Pruett v. State*[262] will undoubtedly have a great impact on criminal law and procedure. In *Pruett*, the defendant[263] had been convicted of capital murder and sentenced to death. Thereafter, he proceeded through all appropriate channels of appeal[264] but was consistently denied relief[265] until he reached the United States District Court for the Northern District of Mississippi,[266] whereupon he was granted habeas relief.[267] The district court's order directed that Pruett be released from custody if he was not retried within 120 days.[268] Upon the passing of the time limit, Pruett petitioned the Circuit Court of Hinds County for release in accordance with the habeas order, but this request was denied.[269] He consequently filed an emergency petition with the supreme court.[270] In affirming the circuit court's decision, the court reasoned that the purpose of a conditional habeas relief grant is to allow a state to hold a prisoner for a specified period even though the conviction is invalid.[271] Further, upon the passing of the conditional time limit, the habeas releasee, still under a valid indictment, may be treated, and tried, as any other prisoner.[272] In effect, the releasee is rearrested and retried under the same indictment. Consequently, the court held that although the prescribed time limit had passed, the state was within its power to rearrest and retry Pruett.

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[261] Those cases not discussed textually are Cole v. State, 525 So. 2d 365, 367 (Miss. 1987)(where witness' name not given to opposing side prior to trial, opposing side must be given opportunity to become familiar with witness' testimony); Lambert v. State, 518 So. 2d 621, 625 (Miss. 1987)(justice court judge commits embezzlement when he converts designated money orders to his own use); Burney v. State, 515 So. 2d 1154, 1660-612 (Miss. 1987)(judge's decision on venue motion warrants wide discretion); Dixon v. State, 513 So. 2d 951, 953-54 (Miss. 1987)(where defendant acquitted and later tried on different change concerning same evidence, double jeopardy has been violated); Williamson v. State, 512 So. 2d 868, 873-74 (Miss. 1987)(where defendant denied right to confrontation, case will be remanded); Shook v. State, 511 So. 2d 1386, 1387 (Miss. 1987)(trial judge's fixing of bail will not be disturbed unless manifestly wrong); McCurdy v. State, 511 So. 2d 148, 150 (Miss. 1987)(where subpoenaed witness fails to appear at trial, counsel may not later argue error where he failed to then move for continuance); Harris v. State, 500 So. 2d 465, 465 (Miss. 1987)(where assignments of error have no merit, conviction will be affirmed).

[262] 512 So. 2d 680 (Miss. 1987).

[263] The defendant, Marion Albert Pruett, was convicted of capital murder in the Circuit Court of Lowndes County and sentenced to death. The supreme court affirmed this conviction on February 23, 1983. Pruett v. State, 431 So. 2d 1101 (Miss. 1983). His petition for writ of certiorari to the United States Supreme Court was denied on March 28, 1983. Pruett v. Mississippi, 464 U.S. 865 (1983).

[264] *Pruett*, 512 So. 2d at 690.

[265] *Id.*

[266] *Id.*

[267] *Id.* The district court granted the petition for habeas corpus relief upon finding there to have been an error during the guilt phase of Pruett's trial. *Id.* The district court conditioned the order stating that if Pruett was not retried within 120 days from the date of the order, he was to be released. *Id.* All agreed that the 120 day limit expired on April 3, 1987. *Id.*

[268] *Id.*

[269] *Id.* at 690-91.

In a strongly worded dissent, Justice Robertson refused to agree with the majority because, in his view, the effect of the time limit is to give a State time during which to appeal the limitation, and failing to take this action, the State is forever procedurally barred from retrying the prisoner.[273] Even more important than this, in Justice Robertson's opinion, is the effect of the Supremacy Clause which forbids a State to ignore time limitations imposed by the federal system.[274]

Martha Bost
Stuart G. Kruger
Beth Anne Levine

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[270] *Id.* at 691.

[271] *Id.* at 691-92.

[272] *Id.* at 692.

[273] *Id.* at 693-94 (Robertson, J., dissenting).

[274] *Id.* at 694.

MISCELLANEOUS

I. Family Law

In 1987, the Mississippi Supreme Court rendered decisions in the area of family law concerning the issues of alimony,[1] adoption,[2] child custody,[3] child support,[4] divorce actions,[5] paternity actions[6] and miscellaneous other topics.[7] For purposes of this review, only those decisions having a notable impact on the status of Mississippi law in the family law area will be textually discussed.

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[1] *See* McNally v. McNally, 516 So. 2d 499 (Miss. 1987)(textually discussed); Banks v. Banks, 511 So. 2d 933, 935 (Miss. 1987)(oral pronouncement by chancellor does not constitute final judgment; thus, chancellor retains right to modify court order); Skinner v. Skinner, 509 So. 2d 867 (Miss. 1987)(textually discussed).

[2] *See In re* Adoption of R.M.P.C., 512 So. 2d 702, 706 (Miss. 1987)(decree of adoption may not be challenged on basis of statutory compliance if defects are not raised within six months of entry of decree); *In re* J.D., 512 So. 2d 684, 686 (Miss. 1987)(abandonment requires intent to forego parental duties, relinquish parental claims to child before parent is denied right to contest adoption proceeding); *In re* B.B. and G.B., 511 So. 2d 918, 919-21 (Miss. 1987)(25 U.S.C. § 1911(a) gives Indian tribe jurisdiction over child custody proceedings which involve child residing or domiciled on reservation; twins born in Harrison County never resided or were domiciled on reservation so as to invoke jurisdiction).

[3] *See* Roberts v. Fuhr, 523 So. 2d 20, 26 (Miss. 1987)(ne exeat writ and bond gave chancery court continuing jurisdiction over child custody proceedings under UCCJA so as to enable them to enforce prior court order despite foreign court order to contrary); Pace v. Owens, 511 So. 2d 489, 490-92 (Miss. 1987)(insufficient evidence to show material change in circumstances which justified change in custody; on remand court ordered lower court to determine if material change in circumstances had in fact occurred so as to justify custody modification); Milam v. Milam, 509 So. 2d 864, 866 (Miss. 1987)(unfitness of mother is sufficient ground to justify modification of child custody decree); Hobbs v. Hobbs, 508 So. 2d 677, 680 (Miss. 1987)(under UCCJA, chancellor proceedings may be initiated); Laskosky v. Laskosky, 504 So. 2d 726, 730 (Miss. 1987)(custody decree of foreign country will be honored if jurisdictional basis was constitutionally sound and decree does not offend UCCJA).

[4] *See* Hull v. State Department of Public Welfare, 515 So. 2d 1205, 1207 (Miss. 1987)(Department of Public Welfare has statutory right to sue so as to enforce child support decrees for indigent children).

[5] *See* Miller v. Miller, 512 So. 2d 1286, 1288 (Miss. 1987)(handwritten letter as answer to divorce complaint which is sent to chancery clerk will suffice to establish personal jurisdiction over author); Jordan v. Jordan, 510 So. 2d 131, 132 (Miss. 1987)(chancellor was not manifestly wrong in granting divorce based on uncondoned adultery); Rasco v. Estate of Rasco, 501 So. 2d 421, 423-24 (Miss. 1987)(divorce, property settlement may well impliedly revoke prior will if testator's intent is shown by clear, unequivocal evidence); Day v. Day, 501 So. 2d 353, 355 (Miss. 1987)(party must prove systematic, continuous behavior before securing divorce on grounds of habitual cruel, inhuman treatment; mere incompatibility will not suffice).

[6] *See* Johnson v. Ladner, 514 So. 2d 327, 328-29 (Miss. 1987)(under Mississippi statute, defendant only may make motion to order blood tests of mother, child, alleged fa-

A. *Alimony*

In *McNally v. McNally*,[8] the Mississippi Supreme Court considered whether a chancery court should retain jurisdiction over alimony questions in view of the fact that economic benefits derived from professional training were sure to emerge in the future.[9] Leo McNally, Jr., and Cecile McNally were married on May 29, 1976. In 1980, the McNallys purchased a home in Jackson and Mr. McNally began dental school.[10] Having received an associate's degree in nursing, Cecile McNally provided the majority of the financial support necessary to maintain the family[11] while Leo McNally was in dental school.[12] Upon graduation, Leo McNally accepted employment on the Mississippi Gulf Coast.[13] Relying on Mr. McNally's decision to move to the coast, Mrs.

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ther in course of paternity action); Varnell v. Green, 512 So. 2d 903, 904 (Miss. 1987)(court refused to take judicial notice of assertion that female cannot become pregnant during her menstrual cycle); Ivy v. ICG R.R. Co., 510 So. 2d 520, 522-24 (Miss. 1987)(meaning of children as used in 45 U.S.C. § 59 includes both legitimate and illegitimate children under Mississippi law; however, illegitimate child must establish paternity in accordance with Mississippi statutes); Clark v. Whiten, 508 So. 2d 1105, 1107, 1108-09 (Miss. 1987)(six-person jury is acceptable in paternity action; individual seeking attorney fees must prove necessity of service, reasonableness of fee); Baker v. Williams, 503 So. 2d 249 (Miss. 1987)(textually discussed).

[7] *See* Cooper v. Keyes, 510 So. 2d 518, 519 (Miss. 1987)(cessation of voluntary payments not required by property settlement is not grounds for contempt order); Regan v. Regan, 507 So. 2d 54, 56-57 (Miss. 1987)(funds derived from personal injury claim belong solely to claimant; hence, such funds cannot be part of property settlement under divorce decree); O'Neill v. O'Neill, 501 So. 2d 1117, 1118-19 (Miss. 1987)(chancellor had authority to exercise discretion in releasing wife from obligation to pay house note; likewise, equity endorsed decision to burden husband with past due as well as future note payments since he had moved into home).

[8] 516 So. 2d 499 (Miss. 1987).

[9] *Id.* at 499-500.

[10] *Id.* at 500.

[11] *Id.* Cecile McNally received an associate nursing degree from Jefferson Davis Junior College before marriage. *Id.* The record from the trial court indicated that Mrs. McNally's income for the period of marriage was approximately $135,000 to $140,000. *Id.* at 501. However, Mr. McNally accounted for only $65,000 of income during the marriage. *Id.* Thus, Cecile contributed approximately twice as much financial support to the marriage than did her husband, Leo. This factor was a strong consideration in the court's decision to allow a retention of jurisdiction. *Id.* at 503.

[12] *Id.* at 501. Leo was in dental school from 1980 to 1984. *Id.*

[13] *Id.* at 500.

McNally resigned her job in Jackson and accepted a lower paying job in Gulfport, Mississippi.[14] Shortly after Mrs. McNally's decision, the divorce saga began.[15]

Both parties originally filed for divorce on the basis of habitual cruel and inhuman treatment.[16] In her complaint, Mrs. McNally requested relief in the form of child custody, child support and alimony.[17] On May 9, 1985, the chancery court granted Cecile McNally a divorce and accordingly awarded her various relief[18]; however, a request for periodic or lump sum alimony was specifically denied.[19] The decision not to award alimony was based upon the fact that such an award would have placed an undue burden on Mr. McNally in view of his strained financial status.[20]

On appeal, Mrs. McNally asserted that equity demanded a nominal award of alimony so as to secure a modification right in the event Mr. McNally's financial status improved.[21] In addressing this assertion, the court granted that *Taylor v. Taylor* [22] in fact "implied that a divorce judgment may not be modified, post-divorce, to include alimony where alimony was not a part of the original judgment."[23] Such an implication, noted the court, was the direct cause of frequent nominal awards of alimony.[24] Obviously, an award of one dollar for alimony solely for the purpose of retaining jurisdiction so as to allow for future modifications makes no sense. Thus, the Mississippi Supreme Court established a new approach for retaining jurisdiction — if subsequent events will likely result in an improved financial status so as to justify an alimony award,[25] a chancery court may *expressly* retain jurisdiction over the alimony question without granting nominal alimony.[26] Therefore, chancery courts in Mississippi no longer must award nominal alimony so as to secure an ability to later modify alimony awards under appropriate circumstances.

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[14] *Id.* As a nurse in Jackson, Cecile McNally made about $1500 per month. However, the employment in Gulfport paid Cecile only $1000 per month. *Id.* As the position in Jackson was filled by the time Cecile discovered Leo's desire for a divorce, she felt it necessary to follow through on her plans to move to Gulfport. *Id.*

[15] *Id.*

[16] *Id.* Mr. McNally initiated the divorce proceedings on July 30, 1984. As a basis for the divorce, Mr. McNally asserted irreconcilable differences. Mrs. McNally answered and filed a counter-claim for divorce on the basis of habitual cruel and inhuman treatment. As a result of such counterclaim, Mr. McNally amended his complaint and alleged habitual cruel and inhuman treatment as a basis for divorce. *Id.*

[17] *Id.* On February 11, 1982, a child, Jamie, was born unto the McNallys. *Id.* at 500.

[18] *Id.* at 501. Cecile was awarded custody of Jamie, the McNally's child, and Leo was ordered to pay $300 per month as child support. Also, the divorce decree required Leo to maintain medical and hospitalization insurance for Jamie. Cecile was given possession of the family car and was charged with the responsibility of paying for it. As to all other outstanding debts which arose during the marriage, Leo was obliged to satisfy them. *Id.*

[19] *Id.*

[20] *Id.* The court noted that at the time for trial, Leo's monthly expenses exceeded his monthly income by approximately $1,000.00. *Id.* However, the court also stated that Leo's inability to pay alimony was clearly outweighed by Cecile's need for alimony. *Id.*

[21] *Id.* at 502. The equities relied upon by Mrs. McNally varied. First, Mrs. McNally had incurred a $500.00 per month reduction in pay by relying upon Mr. McNally's decision to move to Gulfport. *Id.* Also, Mrs. McNally had supported Mr. McNally during his enrollment in dental school. *Id.* at 503. Additionally, and perhaps the most important factor, Mr. McNally's financial status was sure to improve over time and such improvement would be a direct result of educational opportunities supported by Mrs. McNally. *Id.*

[22] 478 So. 2d 310, 312 (Miss. 1985).

In addition to *McNally*, the Mississippi Supreme Court issued two other noteworthy opinions dealing with alimony awards. In *Skinner v. Skinner*,[27] the court concluded by implication that an award of periodic alimony could not be terminated upon the recipient's achieving some arbitrary age limit.[28] Mary Skinner was granted a divorce from

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[23] *McNally*, 516 So. 2d at 502. *See also* Savell v. Savell, 290 So. 2d 621, 624 (Miss. 1974)(implication that alimony must be awarded to retain jurisdiction for subsequent modifications of alimony). However, the court did note that it had never expressly held that some award of alimony in the initial divorce decree was necessary before a chancellor could entertain a subsequent motion to modify. *McNally*, 516 So. 2d at 502.

[24] *McNally*, 516 So. 2d at 502. The practice of awarding nominal alimony so as to retain jurisdiction is not unique to Mississippi. *See, e.g.*, Owens v. Owens, 435 So. 2d 1316, 1319 (Ala. 1983)(nominal alimony awarded to insure subsequent opportunity to modify such); Sands v. Sands, 448 A.2d 822, 826 n.5 (Conn. 1982)(same); Rose v. Rose, 340 S.E.2d 176, 180 (W. Va. 1986)(same).

[25] *McNally*, 516 So. 2d at 502. The court noted that an ability to practice dentistry would clearly result in an improved financial status over the years. *Id.* It is unclear whether the court's holding in *McNally* will apply outside of the professional relationship context. However, there is no reason why *McNally* should not apply if subsequent events are likely to render alimony appropriate, no matter what the context.

[26] *Id.* In reaching this conclusion, the court relied on Moore v. Moore, 401 So. 2d 841, 842 (Fla. App. 1981). In *Moore*, the Florida court authorized *expressed* reservations of jurisdiction without nominal alimony awards. *Moore*, 401 So. 2d at 842.

Also, the Mississippi Supreme Court emphasized that the principle of retaining jurisdiction for modification purposes was not a new approach in Mississippi domestic relations law. *See, e.g.*, Covington v. Covington, 459 So. 2d 780, 782 (Miss. 1984)(in personam jurisdiction subjects one to future modifications of divorce decrees); Tucker v. Tucker, 453 So. 2d 1294, 1297 (Miss. 1984)(retention of jurisdiction appropriate so as to modify child custody in event of material change in circumstances); Campbell v. Campbell, 357 So. 2d 129, 130 (Miss. 1978)(alimony awards subject to future modification).

[27] 509 So. 2d 867 (Miss. 1987).

[28] *Id.* at 869.

William Skinner on the grounds of habitual cruel and unusual punishment.[29] In accord with such divorce, Mr. Skinner was ordered to pay $2,158.52 in periodic alimony until the death or remarriage of Mrs. Skinner or until Mrs. Skinner reached the age of sixty-five.[30] Additionally, a $75,000 lump sum alimony award was ordered to be paid by Mr. Skinner when Mrs. Skinner became sixty-five years of age.[31]

On appeal, Mrs. Skinner questioned the duration of the alimony awards.[32] Relying upon *Wray v. Wray*,[33] the court noted that as a general rule alimony was only to terminate upon death or remarriage.[34] By concluding that the sixty-five year limitation was invalid, the court impliedly held that the establishment of arbitrary age limits as termination dates for alimony was not appropriate.[35] Likewise, the court stated that absent reasonable grounds for delaying lump sum alimony, immediate payment of such was mandated.[36]

Also, in *Banks v. Banks*,[37] the court stated that an oral pronouncement of the alimony to be awarded did not constitute a final judgment and hence, the chancellor retained the right to modify the alimony award.[38]

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[29] *Id.* at 867.

[30] *Id.* at 868.

[31] *Id.* The court noted that Mr. Skinner's assets were between $700,000 and $900,000 at the time of divorce. *Id.* However, Mrs. Skinner had accumulated a mere $40,000 in assets during the marriage. This amount reflected her one-half interest in the marital home. *Id.* In view of this inequity, the court stated that a concurrent award of lump sum and periodic alimony was permissible if the husband had accumulated substantial assets during the marriage. *Id.* at 869.

[32] *Id.* at 867. Also, Mrs. Skinner voiced objection to the amount of alimony awarded. *Id.* However, the court noted that the award did not constitute an abuse of discretion by the chancellor and thus was to be affirmed. *Id.* at 869; *see* Tutor v. Tutor, 494 So. 2d 362, 365 (Miss. 1986)(amount of periodic alimony award did not constitute abuse of discretion).

[33] 394 So. 2d 1341 (Miss. 1981).

[34] *Skinner*, 509 So. 2d at 869. Additionally, the court has the authority to modify alimony awards under appropriate circumstances. *See* East v. East, 493 So. 2d 927, 931 (Miss. 1986)(court has discretionary authority to modify alimony award).

[35] *Skinner*, 509 So. 2d at 869. The court's decision was premised on an attempt to enforce the fundamental purpose of an alimony award. *Id.* As noted by the court, Mrs. Skinner's ability to provide for herself would be greatly diminished upon reaching age 65, and it was at this point in time that alimony would be needed most. *Id.* However, the court did imply that "extenuating circumstances" may well justify the termination of alimony payments at some arbitrary point in time. *Id.* Significantly, Mr. Skinner enjoyed a sound financial basis and thus could easily be charged with a continuing alimony obligation. *Id.*

[36] *Id.* The court made no effort to explain what may constitute reasonable grounds.

[37] 511 So. 2d 933 (Miss. 1987).

B. Paternity

In 1987, the Mississippi Supreme Court addressed the issue of paternity in five cases.[39] The case of *Baker v. Williams*[40] is the only paternity case discussed textually herein. The first issue of importance in *Baker* was whether a legitimate child could advance a paternity action by and through her mother on the basis of section 93-9-9 of the Mississippi Code.[41] Julie Baker, a minor child, was born to the marriage of Leland Baker and Caroline Baker.[42] Mr. and Mrs. Baker were subsequently divorced, and custody of Julie was awarded to Caroline Baker.[43] After the divorce, Caroline remarried Charles W. Williams.[44] Mr. Williams attempted to adopt Julie but such attempt was contested by the presumed natural father, Leland Baker.[45] Thus, Julie, the minor child, filed a petition, by and through her mother, Caroline, to establish her stepfather, Charles Williams, as her true natural father.[46] The chancellor dismissed the petition on the basis of res judicata, estoppel, and laches as the result of prior divorce proceedings.[47]

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[38] *Id.* at 934-35. In *Banks*, the chancellor orally expressed an inclination to increase alimony by $500 per month. However, when the chancellor filed a final judgment, only a $250 per month increase was allowed. *Id.* The court relied upon MISS. R. CIV. P. 54(a) as well as Jackson v. Schwartz, 240 So. 2d 60, 61-62 (Miss. 1970), to conclude that a chancellor's judgment was not final until "signed by the judge and filed with the clerk for entry on the minutes." *Banks*, 511 So. 2d at 935.

[39] *See supra* note 6.

[40] 503 So. 2d 249 (Miss. 1987).

[41] *Id.* at 252. Section 93-9-9 of the Mississippi Code provides: "Paternity may be determined upon the petition of the mother, the child, or any public authority chargeable by law with the support of the child . . . ." MISS. CODE ANN. § 93-9-9 (1972).

[42] *Baker*, 503 So. 2d at 251. Julie Baker was one of two children born to the marriage of Leland and Caroline Baker. *Id.* A certified birth certificate, signed by Caroline Baker Williams, represented Leland Baker to be the natural father of Julie Baker. *Id.* at 252.

[43] *Id.* at 252. In accord with the divorce decree, Leland Baker enjoyed visitation rights and made child support payments for eleven years. *Id.* During the course of the divorce proceedings, Caroline Baker Williams expressly stated that Julie Baker was "born of this marriage" (the marriage between Caroline and Leland Baker). *Id.*

[44] *Id.* at 251. Julie resided with Caroline and Charles Williams after the marriage. The record indicates that Mr. Williams likewise provided support for Julie. *Id.*

[45] *Id.* The proceeding was dismissed pursuant to MISS. CODE ANN. § 93-17-7 (Supp. 1987).

[46] *Baker*, 503 So. 2d at 251. The petition was filed pursuant to the Mississippi Uniform Law on Paternity. *See* MISS. CODE ANN. § 93-9-1 et seq. (1972)(Mississippi Uniform Law on Paternity). Both Leland Baker and Charles Williams were named defendants. However, the petition asserted that Charles Williams was in fact the natural father of Julie Baker. *Baker*, 503 So. 2d at 251.

On appeal, the Mississippi Supreme Court, in a 4-4 decision, concluded that a legitimate child could question paternity under section 93-9-9 of the Mississippi Code.[48] The majority noted that although the probable intent of the statute was to provide illegitimate children a means of establishing paternity, no apparent prohibition existed to prevent a legitimate child from utilizing the statute.[49] However, in a strongly worded dissent, Justice Griffin noted that the effect of such a holding was to allow a parent to bastardize a child.[50] Relying on *Graham v. Lee*,[51] Justice Griffin stated that attempts to bastardize children born in lawful wedlock are against public policy and common decency.[52] Additionally, Justice Griffin argued that the true purpose of

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[47] *Baker*, 503 So. 2d at 251. In a prior divorce action, Caroline Baker specifically stated that Julie had been born unto the marriage of herself and Leland Baker. On this basis, the chancellor concluded that the doctrine of res judicata operated to prevent the retrial of the issue of paternity. *Id.* Furthermore, the chancellor found that a representation on a birth certificate by Caroline Baker that Leland was the father of Julie, effectively estopped a second trial on the issue of paternity. *Id.* As to the laches argument, the chancellor stated that the eleven year period in which Caroline accepted child support payments from Leland constituted laches and prevented a relitigation of paternity. *Id.*

[48] *Id.* at 252; *see supra* note 41.

[49] *Baker*, 503 So. 2d at 252. The court began by recognizing the sanctity of the family relationship in our society. *Id.* at 251. However, the fact that the statute at issue was being used to destroy the family structure was simply not controlling. In accord with Palmer v. Mangum, 338 So. 2d 1002 (Miss. 1976), the court concluded that if a child were properly before the court and advanced a claim upon which relief could be granted, presumed legitimacy would not prevent a paternity action. *Baker*, 503 So. 2d at 251.

Furthermore, the court noted that policy considerations were not controlling in two analogous decisions. *See* Grimsley v. Tyner, 454 So. 2d 482, 483-85 (Miss. 1984)(putative father has right to file petition for filiation); Palmer v. Mangum, 338 So. 2d 1002, 1003-04 (Miss. 1978)(action to enforce child support obligations may be advanced by minor after achieving age of one year).

[50] *Baker*, 503 So. 2d at 255-59 (Griffin, J., dissenting). Justice Griffin founded his dissent on the basis of public policy and common decency. *Id.*

[51] 204 Miss. 416, 37 So. 2d 735 (1948).

[52] *Baker*, 503 So. 2d at 256 (Griffin, J., dissenting). In *Graham*, a husband and wife separated when the husband discovered that the wife was engaged in an adulterous relationship with Graham. Almost nine months after the separation, a child was born to the wife. At this time, the wife was living with Graham. Shortly after birth, Graham adopted the child without giving notice to the husband. One year later, the wife secured a divorce from the husband. Approximately two years later, the wife returned home to the husband bringing the child along. *Graham*, 204 Miss. at 429-30, 37 So. 2d at 736-37.

In view of the wife's departure, Graham filed suit in an attempt to gain custody of the child. The husband and wife jointly petitioned the court to vacate the prior adoption. *Id.* In *Graham*, the court concluded that "as a matter of policy, no outsider will be the paternity act was to provide the mother with a means of securing child support.[53] Clearly, there was no need for child support in *Baker* as both defendants had willfully provided support in the past. In conclusion, Justice Griffin stated that the legislative intent of section 93-9-9 could not have embraced the purpose for which Caroline Baker Williams invoked it,[54] a position the majority seemed uncertain about.[55]

Upon establishing standing in Julie Baker, the minor child, the court addressed the merits of the appeal.[56] The court concluded that res judicata, estoppel, and laches could not be asserted on the basis of a prior divorce decree because the minor child was not a party to such proceedings.[57] Likewise, the actions of Julie's mother could not be imputed to her so as to stop this cause of action.[58] In view of the 4-4 split in this decision, it would be wise to keep watch over the legislature in search of clarification for section 93-9-9 of the Mississippi Code.

II. Wills and Estates

In the area of wills and estates, the Mississippi Supreme Court addressed the issues of undue influence,[59] ancillary administration,[60]

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permitted to attempt to prove" the illegitimacy of a child born to a lawful husband and wife. *Id.* at 432, 37 So. 2d at 737-38. Also, the court noted that "public policy and common decency are opposed to the bastardizing of children born in wedlock against the wishes and against the protest of the putative parents . . . ." *Id.*; *see Ex Parte* Madalina, 174 Cal. 693, 164 P. 348 (Cal. 1917)(public policy is against outsider questioning legitimacy of child).

[53] *Baker*, 503 So. 2d at 257-59 (Griffin, J., dissenting). Justice Griffin relied upon Kendrick v. Everheart, 390 So. 2d 53 (Fla. 1980) which stated, ". . . the purpose of the paternity statute is to provide a natural mother with a judicial mechanism for obtaining child support from the natural father rather than to provide a putative father with a means to prove his own paternity." *Kendrick*, 390 So. 2d at 55-56. With the stated purpose in mind, Justice Griffin noted that the plaintiff had improperly invoked the paternity statute since both defendants, the presumptive father and the stepfather, were satisfying their duty to provide child support. *Baker*, 503 So. 2d at 258.

[54] *Baker*, 503 So. 2d at 259 (Griffin, J., dissenting).

[55] *Id.* at 252. The court noted that the question presented herein may well be "a case for legislative discussion." *Id.*

[56] *Id.* at 254-55; *see supra* note 47 and accompanying text.

[57] *Baker*, 503 So. 2d at 254-55. The court noted that when "dealing with the prospective rights of a minor child to establish paternity, the child, if not formally a party, is not bound by a paternity determination in a marital dissolution action." *Id.* at 254; *see* Ruddock v. Ohls, 91 Cal. App. 2d 271, 154 Cal. Rptr. 87,91 (1979)(minor child not bound by paternity determination in divorce decree); *see also* Standard Oil v. Howell, 360 So. 2d 1200, 1202 (Miss. 1978)(four elements of doctrine of res judicata).

[58] *Baker*, 503 So. 2d at 255. *See* Wilson v. Wilson, 464 So. 2d 496, 498 (Miss. 1985)(mother's actions not to be imputed to child).

[59] *See In re* Estate of Haney, 516 So. 2d 1359, 1361 (Miss. 1987)(discussion of undue

claims against the estate grounded in quantum meruit,[61] inventory of estate assets,[62] right of renunciation,[63] fraudulent omission of a known heir by an administratrix,[64] statute of limitations,[65] will construction[66] and others.[67]

A. *Undue Influence*

In *Costello v. Hall*,[68] the Mississippi Supreme Court considered whether or not the grant of a power of attorney creates a confidential relationship so as to give rise to the presumption that undue influence in fact existed.[69] Linnie Hall, the testator in *Costello*, executed a will

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influence as grounds for contesting will); Blissard v. Estate of White, 515 So. 2d 1196, 1199 (Miss. 1987)(rebuttable presumption of undue influence created where primary beneficiary of will was granted power of attorney by testatrix); Sacco v. Gordon, 515 So. 2d 906, 909 (Miss. 1987)(no confidential relationship established so as to raise presumption of undue influence); Anderson v. Burt, 507 So. 2d 32, 36 (Miss. 1987)(rebuttable presumption of undue influence exists where grantor conveys property to one who owes him fiduciary duty); Costello v. Hall, 506 So. 2d 293 (Miss. 1987)(discussed textually).

[60] *See In re* Estate of Waitzmann, 507 So. 2d 24, 26 (Miss. 1987)(beneficial interests in trust are personal rather than real property; judgment of sister state has res judicata effect on validity of will bequeathing those interests).

[61] *See* Estate of Johnson v. Adkins, 513 So. 2d 922, 925-26 (Miss. 1987)(claimant must have had reasonable expectation of compensation to recover reasonable value of materials/services rendered from testator's estate).

[62] *See In re* Estate of Holloway, 515 So. 2d 1217, 1222-23 (Miss. 1987)(statutory presumption of survivorship under Miss. Code Ann. § 81-1-63 (Supp. 1987) does not apply to certificates of deposit; absent valid intervivos gift, certificates may be part of testator's estate).

[63] *See* Shattuck v. Tyson, 508 So. 2d 1077, 1080-81 (Miss. 1987)(right to renounce will is personal right which must be exercised by beneficiary during his lifetime providing some provision for beneficiary is made in will).

[64] *See* Smith v. Estate of King, 501 So. 2d 1120, 1122-23 (Miss. 1987)(fraudulent omission of known heir by administratrix will prevent 90 day time limit from running against illegitimate).

[65] *See In re* Estate of Philyaw, 514 So. 2d 1232, 1236-37 Miss. 1987)(time for appeal of chancellor's ruling concerning contested claims begins to run from date of ruling, not from date estate is closed); *In re* Heirship of McLeod, 506 So. 2d 289, 291-92 (Miss. 1987)(potential heir need not bring suit to determine heirship until question of such status arises).

[66] *See* Ross v. Brasell, 511 So. 2d 492, 495 (Miss. 1987)(ambiguous terms of will may be explained by extrinsic evidence to determine true intent of testator).

[67] *See* Estate of Manscoe v. Simmons, 512 So. 2d 682, 683-84 (Miss. 1987)(claim against estate must have been enforceable against decedent during his lifetime to be valid); *In re* Estate of Davis, 510 So. 2d 798, 799-800 (Miss. 1987)(chancery clerk has authority to admit will to probate; grant letters testamentary).

[68] 506 So. 2d 293 (Miss. 1987).

[69] *Id.* at 296-97. The confidential relationship doctrine was first addressed by the

leaving the majority of her estate to her brother, Marion Costello, while bequeathing a mere $10.00 to her husband, W.C. Hall.[70] Along with the execution of the last will and testament of Linnie Hall, a new general power of attorney was granted by Mrs. Linnie Hall in favor of Marion Costello.[71] Pursuant to this power of attorney, Costello added himself to Mrs. Hall's savings account. Shortly after her death[72] he withdrew the funds held in her savings account, paid off an outstanding loan and transferred the balance to his own personal account.[73] Upon discovery of Mr. Costello's actions, Mr. Hall initiated proceedings which resulted in a finding by the trial court that the power of attorney granted Mr. Costello gave rise to a fiduciary relationship resulting in a presumption of undue influence.[74] Furthermore, the trial court concluded that Mr. Costello failed to prove by clear and convincing evidence the absence of undue influence, as required by *Murray v. Laird*,[75] and hence, the will was found invalid.[76]

Mississippi Supreme Court in Croft v. Alder, 237 Miss. 713, 723, 115 So. 2d 683, 688 (1959). In *Croft*, the court noted that a confidential relationship arose when a beneficiary exerted dominant influence over the testator. *Croft*, 237 Miss. at 722-23, 115 So. 2d at 686-89. Furthermore, if the beneficiary abused the confidential relationship for his own personal gain, a presumption arises that the beneficiary has exerted undue influence. *Id.* at 723, 115 So. 2d at 688.

[70] *Costello*, 506 So. 2d at 294. Linnie Hall married W.C. Hall on April 4, 1970. *Id.* Both Linnie and W.C. were problem drinkers. *Id.* at 295. The evidence presented at the trial court revealed that W.C. was not the most caring husband and Linnie even, at one point in time, filed for divorce. *Id.* In early 1981, Linnie Hall executed her first will, with the help of an attorney, in which W.C. Hall was devised one-fourth interest in her real estate. *Id.* Shortly after the execution of the first will, Linnie executed a second will, this time leaving W.C. a mere $10.00. *Id.*

[71] *Id.* at 295. Pursuant to a request by Costello, the last will and testament of Linnie Hall was executed on September 15, 1982. *Id.* At such time, Mrs. Hall was in the hospital; however, a Dr. Hatten examined her and determined that she was competent to execute the will. *Id.* The attorney, Mr. Terry, took full responsibility for having the will executed and Mr. Costello was in no way involved with the execution process. *Id.* The new power of attorney was executed at the request of Mr. Terry due to an alleged change in the law without the knowledge and consent of Mr. Costello. *Id.*

[72] *Id.* at 296. Mrs. Hall died on September 30, 1982. The death followed a long illness which resulted from continuous alcoholic intake. Mr. Hall never attempted to visit Mrs. Hall during the course of her hospitalization. However, Mr. Costello was a constant companion of Mrs. Hall during her final days. *Id.*

[73] *Id.* The personal account of Mr. Costello was located in Spokane, Washington. *Id.*

[74] *Id.*

[75] 446 So. 2d 575 (Miss. 1978). A proponent of a will which has been encumbered by a presumption of undue influence must prove three elements: 1) good faith of the beneficiary; 2) full knowledge and deliberation by grantor of his actions; 3) independent advise from a detached and disinterested individual. *Id.*; *see also* Harris v. Sellers, 446 So. 2d 1012, 1014-15 (Miss. 1984)(factors to be proven so as to rebut presumption of undue

On appeal, Mr. Costello alleged that the trial court erred in finding a confidential relationship which gave rise to a presumption of undue influence.[77] The Mississippi Supreme Court noted that the question of whether the mere granting of a power of attorney alone would give rise to a presumption of undue influence was a case of first impression in Mississippi. Although the case of *Weston v. Estate of Lawler*[78] involved a power of attorney granted by the testator, the court noted that *Weston* did not justify a presumption of undue influence on the basis that a confidential relationship existed due to a power of attorney.[79] After recognizing an obvious split in authority among states on the issue of whether a power of attorney created a confidential relationship per se,[80] the court concluded that without additional evidence to establish some impure motive on behalf of a grantee, the mere grant of a power of attorney did not create a confidential relationship.[81]

Absent the existence of a confidential relationship as a matter of law, the court reiterated that a dominant, overpowering personality must exist before a confidential relationship arises.[82] Also, assuming

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influence). *But cf.* Mullins v. Ratcliff, 515 So. 2d 1183, 1193 (Miss. 1987)(third prong of test now requires showing of independent consent, action; not advise from competent person).

[76] *Costello*, 506 So. 2d at 296.

[77] *Id.*

[78] 406 So. 2d 31 (Miss. 1981), *aff'd*, 451 So. 2d 739 (Miss. 1984).

[79] *Costello*, 506 So. 2d at 297. The court noted that other relevant factors gave rise to the presumption in *Weston*. Specifically, the grantor of the power occupied the same house and was in close daily contact with the grantee. *Id.*

[80] *Compare* Parker v. Spurlin, 179 S.E.2d 251, 254-55 (Ga. 1971)(power of attorney creates confidential relationship *per se*) *and* Askew v. Askew, 619 S.W.2d 384, 386-87 (Tenn. App. 1981)(same) *with In re* Estate of MacPhee, 187 So. 2d 679, 681 (Fla. Dist. Ct. App. 1966)(power of attorney merely increases defendant's burden to overcome presumption of undue influence) and *In re* Estate of Herm, 284 N.W.2d 191, 200 (Iowa 1979)(same).

[81] *Costello*, 506 So. 2d at 297. The court noted that to establish a confidential relationship on the basis of a power of attorney, without more, would create a harsh and unjust result. *Id.*; *see* Sacco v. Gordon, 515 So. 2d 906, 909 (Miss. 1987)(no confidential relationship created due to power of attorney). In *Sacco*, the court noted that there must be some overreaching on behalf of the beneficiary so as to establish a confidential relationship. *Id. See generally* Hendricks v. James, 421 So. 2d 1031, 1041 (Miss. 1982)(if dominant influence is exercised over weak, handicapped individual, imposition of fiduciary relationship is appropriate); Barnett v. Barnett, 155 Miss. 449, 457, 124 So. 498, 500 (1929)(confidential relationship established when one substitutes his will for will of another).

[82] *Costello*, 506 So. 2d at 297-99. *See In re* Estate of Haney, 516 So. 2d 1359, 1361 (Miss. 1987)(domination of dependent individual or trust yields confidential relationship). In *Haney*, a grandmother left all of her property to a grandson, pursuant to terms

such a relationship is found, the court noted that an abuse of the relationship must be shown before the presumption of undue influence is raised.[83]

In a second case of importance, *Blissard v. Estate of White*,[84] the Mississippi Supreme Court addressed the elements necessary to be proven to rebut a presumption of undue influence.[85] A beneficiary of a will must show by clear and convincing evidence, good faith, full knowledge and deliberation by the testator, and the testator's independent consent and action.[86]

B. Ancillary Administration

Ancillary administration of a will is the "administration in [a] state where [the] decedent has property and which is other than where [the] decedent was domiciled."[87] In *Davis v. Davis*,[88] the court addressed the issue of ancillary administration.[89] Barbara Davis, the executrix of Helen Waitzman's will, probated a will in Dade County, Florida.[90] The will was contested in Florida by Howard Davis on the grounds of undue influence and testamentary capacity.[91] The Florida court found the will to be valid.[92] As the testator's will devised prop-

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of a will. *Id.* at 1360. A granddaughter alleged that the grandson had unduly influenced the grandmother and hence the will was invalid. *Id.* The court, however, concluded that no confidential relationship existed between the grandmother and her grandson and thus, the will was valid. *Id.* At trial, the grandson put on evidence which portrayed the grandmother as a strong-willed individual and which proved his independence from the execution of the will. *Id.* In *Haney*, the Mississippi Supreme Court concluded that the grandson had not exerted dominant influence over the grandmother and hence, no confidential relationship existed. *Id.* at 1361.

[83] *Costello*, 506 So. 2d at 298-99. *See Sacco*, 515 So. 2d at 909 (abuse of confidential relationship must exist before undue influence is presumed).

[84] 515 So. 2d 1196 (Miss. 1987).

[85] *Id.* at 1200.

[86] *Id.* The third element a beneficiary must prove, independent consent and action, was developed in the case of Mullins v. Ratcliff, 515 So. 2d 1183 (Miss. 1987). Prior to *Mullins*, the third element required the testator to have secured the advice of a competent, independent person. *See* Murray v. Laird, 446 So. 2d 575, 578 (Miss. 1978)(independent advice required).

[87] BLACK'S LAW DICTIONARY 78 (5th ed. 1979).

[88] 507 So. 2d 24 (Miss. 1987).

[89] *Id.* at 24-25.

[90] *Id.* at 24. The testatrix was Helen J. Waitzman who was domiciled in Florida at the time of her death. *Id.*

[91] *Id.*

[92] *Id.*

erty located in Mississippi,[93] Barbara Davis subsequently probated the will in Amite County.[94] Howard Davis followed Barbara Davis to Amite County and once again tried to contest the will.[95] Prior to trial, the parties stipulated that if the property were classified as personal, a second contest would be inappropriate in light of the earlier Florida decision.[96] However, of importance is a statement made by the Mississippi Supreme Court: ". . . our concern lies with legal precedent rather than with the stipulation reached by the individual parties . . . ."[97] Hence, it would seem that the stipulation merits little consideration as the basis for the result reached in *Davis*.

The ultimate issue presented in *Davis* was whether Howard Davis would be allowed to contest the will a second time pursuant to the probate in Mississippi.[98] Section 91-7-33 of the Mississippi Code states that a foreign will "may be contested as the original might have been if it had been executed in this state, or the original will may be proven and admitted to record here."[99] The case of *Heard v. Drennen*[100] interpreted this statute as protecting "the right to contest [the will] when presented here, as the original might have been if it had been executed in this state."[101] Hence, it seems that if a foreign will is probated in Mississippi, the right to contest such is well-founded.

The Mississippi Supreme Court, in *Davis*, concluded that the will in fact could not be contested a second time in Mississippi.[102] The decision was premised on the basis of a lack of jurisdiction as well as the full faith and credit clause.[103] As a general rule, judgments of a foreign state should be enforceable in another state, absent a lack of jurisdiction.[104] A relevant example is found in *Woodville v. Piccanti*,[105] where the Mississippi Supreme Court concluded that a judgment from a foreign state which established a document as a will had no effect as to real property in Mississippi.[106] In *Woodville*, the irrelevancy of an earlier will contest was founded on the fact that the foreign state lacked jurisdiction so as to indorse a devise of Mississippi real property.[107]

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[93] *Id.* at 25. In 1933, the testatrix conveyed in trust, oil, gas and minerals to E.V. Mosely. *Id.* In return, the testatrix received a certificate which recognized her as a beneficial owner of the trust. *Id.* Upon cessation of the trust, individuals holding the certificates were to become the owners of the oil, gas and mineral interests. *Id.* At death, the testatrix owned a 17 ⅓% beneficial interest. *Id.* Hence, the issue was whether the certificates, which ultimately entitled the holder to oil, gas and mineral interests, were classified as real or personal property under Mississippi law. *Id.*

[94] *Id.* at 24.

[95] *Id.*

[96] *Id.* at 24-25.

[97] *Id.* at 25.

[98] *Id.* at 25-26.

[99] Miss. Code Ann. § 91-7-33 (1972).

[100] 93 Miss. 236, 46 So. 243 (1908).

[101] *Id.* at 242, 46 So. at 244. In *Heard*, the court noted that the effect of a foreign probate was only to "dispense with formal proof of the due execution of the will" when subsequently probated in Mississippi. *Id.*; *see also* Belt v. Adams, 125 Miss. 387, 391, 87 So. 666, 668 (1921)(foreign will must be probated in Mississippi to effectively convey property within state); R. Weems, Mississippi Wills and Estates: Cases, Statutes, and Materials 216-219 (1983)(general discussion of foreign will probate).

[102] *Davis*, 507 So. 2d at 26-27.

However, in *Davis*, the court concluded that the property in issue, beneficial interest in certain trust assets,[108] was personal in nature and not real property.[109] Since the property was classified as personal, the court stated that the will contest in Florida collaterally estopped Howard Davis from asserting a second will contest in Mississippi.[110] Significantly, the Mississippi Supreme Court, at the outset of the *Davis* opinion, noted that "we may intervene when disposition of decedent's interest involve property interest which are subject to our jurisdiction."[111] Therefore, the basis of such conclusion apparently was that the court must observe judgments of sister states if such judgments are jurisdictionally sound.[112]

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[103] *Id.* at 25-26. The court noted that Galbraith & Dickens Aviation Insurance Agency v. Gulf Coast Aircraft Sales, Inc., 396 So. 2d 19 (Miss. 1981), allowed a judgment of a foreign state to be attacked only on jurisdictional grounds. *Davis*, 507 So. 2d at 25. Also, the full faith and credit clause under article 4, section 1 of the United States Constitution mandates enforcement of a foreign judgment if such judgment is jurisdictionally sound. *Davis*, 507 So. 2d at 25.

[104] *Davis*, 507 So. 2d at 25. *See also*, *supra* note 103 and accompanying text.

[105] 119 Miss. 442, 81 So. 127 (1919).

[106] *Id.* at 462, 81 So. at 129-30. Clearly, no foreign state has a jurisdictional basis for ruling on a dispute over real property located in Mississippi. *See* R. WEEMS, MISSISSIPPI WILLS AND ESTATES: CASES, STATUTES, AND MATERIALS 217 (1983)(probate of will in domiciliary state has no effect on real estate located in foreign state).

[107] *Woodville*, 119 Miss. at 462, 81 So. at 131-32.

[108] *See supra* note 93 and accompanying text.

[109] *Davis*, 507 So. 2d at 26-27. The court relied on § 1-3-41 of the Mississippi Code, which defines personal property. In reality, Mississippi defines personal property via an exclusionary method — whatever is not real property, is personal property. *See* Watson v. Caffery, 236 Miss. 223, 233, 109 So. 2d 862, 866 (1959)(everything not qualifying as real property is designated personal property). Furthermore, as the testatrix held trust certificates, the court concluded that Crook v. Commercial National Bank & Trust Co., 375 So. 2d 1006 (Miss. 1979) mandated that the certificates be classified as personal property since the holder was only entitled to earnings, proceedings, and managerial imput. *Crook*, 375 So. 2d at 274.

[110] *Davis*, 507 So. 2d at 26-27.

[111] *Id.* at 26. This statement clearly recognizes the court's right to ignore a foreign judgment if the property at issue is subject to Mississippi's jurisdiction only. Thus, this statement would support a conclusion contrary to the one reached in *Davis*, as personal property located in Mississippi and bequeathed in a will passes only in accordance with

The court's holding in *Davis* seems to change a well settled point of law and contradict a relevant Mississippi statute. Section 91-1-1 of the Mississippi Code provides that "all *personal property* situated in this state shall descend and be distributed according to the laws of this state . . . notwithstanding the domicile of the deceased may have been in another state".[113] In *Bolton v. Barnett*,[114] the court in fact held that when dealing with personal property which passes via a will, Mississippi, not a foreign state in which the testator is domiciled, has jurisdiction over personal property located within the state.[115] Thus, it seems as if the Mississippi Supreme Court forgot about a relevant Mississippi statute. No reference was made to the statute throughout the *Davis* opinion. The combination of jurisdiction under section 91-1-1 and right to contest a will when probated in Mississippi, regardless of an earlier probate by a foreign state which lacked jurisdiction, would appear to demand a different result than that reached by the court in *Davis*.

Two apparent reasons for the court's holding in *Davis* come to mind. One, the stipulation, as noted above, agreed that if the property at issue was in fact personal, no right to contest existed.[116] However, the court clearly stated at the outset that such stipulation did not control the reasoning of the court.[117] Two, section 91-1-1 gives Mississippi jurisdiction over personal property bequeathed under a will only if such property is located in Mississippi.[118] The court in *Davis* devotes no time to discussing the location of the personal property and hence,

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Mississippi laws. *See infra* notes 113-118 and accompanying text.

[112] *See supra* notes 103-107 and accompanying text.

[113] MISS. CODE ANN. § 91-1-1 (1972). This statute is a clear departure from common law where personal property passed according to the laws of the domiciliary state. *See* Jahier v. Rascoe, 62 Miss. 699, 704 (1885)(personal property situated in Mississippi at testator's death will pass in accordance with Mississippi laws).

[114] 131 Miss. 802, 95 So. 721 (1923).

[115] *Id.* at 827, 95 So. at 725-26. The court noted that "the chancery court [had] jurisdiction to receive this probate whenever real *or* personal property is located within that county." *Id.* at 823, 95 So. 2d at 723-26; *see also* Ewing v. Warren, 144 Miss. 233, 251, 109 So. 601, 603 (1926)(stock of Mississippi corporation is personal property and passes in accordance with Mississippi's descent and distribution statutes).

[116] *See supra* note 96 and accompanying text.

[117] *See supra* note 97 and accompanying text.

[118] MISS. CODE ANN. § 91-1-1 (1972). *See, e.g.*, Mayo v. Equitable Life Assur. Soc., 71 Miss. 590, 592, 15 So. 791, 793 (1894)(purchase of insurance policy while in Mississippi does not constitute personal property located within state so as to invoke Mississippi's descent and distribution statutes).

one may only wonder if this issue was considered by the court.

III. INSURANCE

In 1987, the Mississippi Supreme Court addressed twelve insurance cases. The following issues were involved: bad faith,[119] contract construction,[120] definition of total disability,[121] mistaken overpayment by an insurance company,[122] existence of a contract,[123] definition of physical contact as used in Mississippi statute,[124] stacking of insurance policies[125] and remittitur of a bad faith punitive damage award.[126] Below, only those cases of first impression or those which clarified Mississippi law will be discussed.

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[119] *See* Life Ins. Co. v. Allen, 518 So. 2d 1189, 1193 (Miss. 1987)(punitive damages properly awarded for failure to honor claim under disability policy); Blue Cross & Blue Shield v. Maas, 516 So. 2d 495, 498 (Miss. 1987)(award of punitive damage was justified by failure to pay legitimate claim); Pioneer Life Ins. Co. v. Moss, 513 So. 2d 927, 930 (Miss. 1987)(absence of arguable reason does not mandate punitive damage award - jury must also find that defendant committed willful, malicious wrong or acted with gross disregard of another's rights).

[120] *See* Scott v. Transport Indemnity Co., 513 So. 2d 889, 894-95 (Miss. 1987)(insurance contract may be orally modified by agent if supported by consideration, detrimentally relied upon); Ford v. Lamar Life Ins. Co., 513 So. 2d 880, 887 (Miss. 1987)(ambiguous contract will be construed in favor of insured; so construed, insured still was not insurable as standard risk); Cherry v. Anthony, 501 So. 2d 416, 419 (Miss. 1987)(contract will be construed in accord with objective standards not unexpressed subjective intent of parties).

[121] *See* Lamar Life Ins. Co. v. Shaw, 502 So. 2d 323, 326 (Miss. 1987)(three elements of total disability - consistent, regular current employment; employee is capable of substantially performing work alone; monetary reward is comparable to previous employment).

[122] *See* U.S.F. & G. Co. v. Newell, 505 So. 2d 284, 287-88 (Miss. 1987)(repayment is mandated unless payee has significantly changed his position in reliance upon overpayment).

[123] *See* Nunley v. Merrill, 513 So. 2d 582, 585 (Miss. 1987)(one not possessing actual or apparent authority in course of agency relationship cannot contractually obligate insurance company).

[124] *See* Southern Farm Bureau Cas. Ins. Co. v. Brewer, 507 So. 2d 369, 370-72 (Miss. 1987)(physical contact between two vehicles includes striking of intermediate object by one which is propelled without intervention into other).

[125] Brown v. Maryland Cas. Co., 521 So. 2d, 856, 857 (Miss. 1987). Currently, a petition for rehearing of *Brown* is pending before the Mississippi Supreme Court. In the event that the original opinion is reaffirmed, *Brown* will provide new alternatives for plaintiffs. Basically, the court in *Brown* concluded that a Class 2 insured could stack coverages held under an uninsured motorist policy. *Id.*

[126] *See* Mutual Life Ins. Co. v. Estate of Wesson, 517 So. 2d 521 (Miss. 1987)(textually discussed).

A. *Remittitur of Punitive Damage Award*

In *Mutual Life Insurance Co. v. Estate of Wesson,*[127] the Mississippi Supreme Court ordered a remittitur of six million five hundred thousand dollars ($6,500,000) from a punitive damage award of eight million dollars ($8,000,000).[128] Dr. and Mrs. Ray Wesson were killed in a plane crash while traveling with the United States Amateur Boxing Team.[129] Prior to his death, Dr. Wesson had secured a life insurance policy from the Mutual Life Insurance Co. [hereinafter MONY].[130] Upon the death of Dr. Wesson, MONY wrongfully refused to honor the policy on the basis of an incorrect belief that the policy had lapsed for failure to pay the premiums.[131] Initially, the court noted that MONY had no "arguable reason"[132] for denying Dr. Wesson's claim and that it was therefore proper to submit the question of punitive damages to the jury.[133] The jury returned a punitive damage award of eight million dollars ($8,000,000) in favor of Dr. Wesson's estate.[134] It was the court's decision to greatly reduce the punitive damage award which makes this case important.

Relying on *Bankers Life & Casualty Co. v. Crenshaw,*[135] the court recognized three general factors to be considered when assessing a punitive damage award:

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[127] 517 So. 2d 521 (Miss. 1987).

[128] *Id.* at 533.

[129] *Id.* at 526. Dr. and Mrs. Wesson were survived by four minor children. *Id.*

[130] *Id.* at 524-27. The insurance policy was dated February 1, 1974. The policy amount was $87,136. *Id.*

[131] *Id.* at 526. When the insurance policy was issued, Dr. Wesson exercised an automatic premium loan provision. This provision would prevent the lapse of the insurance policy due to failure to pay the premium. *Id.* at 524-26. Hence, MONY decided that another provision within the policy effectively negated the automatic premium provision and thus, the policy was issued without the premium provision. *Id.* Subsequently, MONY discovered that they had wrongfully relied on the alternate provision and therefore, the automatic premium provision was operative. *Id.* Accordingly, the policy had not lapsed for failure to pay the premium and MONY's refusal to pay was wrongful. *Id.*

[132] *Id.* at 528. Absent an arguable or legitimate reason for denying a claim, it is proper to submit the issue of punitive damages to the jury. *Id.*; *see* Weems v. American Sec. Ins. Co., 486 So. 2d 1222, 1226-27 (Miss. 1986)(punitive damage issue properly submitted to jury); Aetna Cas. & Sur. Co. v. Steele, 373 So. 2d 797, 801-02 (Miss. 1979)(arguable reason existed so as to defeat punitive damage award); Standard Life Ins. Co. v. Veal, 354 So. 2d 239, 247-49 (Miss. 1977)(no reason existed to justify action of insurance company).

[133] *Mutual Life Ins. Co.*, 517 So. 2d at 529. The court noted numerous facts which supported the conclusion that no "arguable reason" existed and hence, the issue of punitive damages was properly submitted to the jury. *Id.* at 528-29.

[134] *Id.* at 524.

[135] 483 So. 2d 254 (Miss. 1985).

> 1) award should be sufficient to punish the defendant . . . and deter any similar conduct in the future;[136]
> 2) award should make an example of the defendant;[137] and
> 3) jury should consider the economic status of the defendant.[138]

After recognizing such factors, the court found, most interestingly, in light of the ultimate decision,[139] that it was "within the province of the jury"[140] to establish a punitive award.[141] Also, the court stated that the punitive award would "not be disturbed unless for exceptional causes or the amount [was] arbitrary or unreasonable."[142] Therefore, the court apparently should defer to the collective wisdom of a jury absent some clearly identifiable reason which would mandate a reconsideration of the punitive award.

Obviously, the Mississippi Supreme Court believed that "special circumstances" did exist and thus, the punitive award was reconsidered. In addition to the general factors mentioned above[143] the court relied upon *Ford Motor Co. v. Durrill*[144] to establish specific factors to be considered when awarding punitive damages.[145] Such factors are: 1) nature of the wrong; 2) character of the conduct involved; 3) degree of culpability of wrongdoer; 4) situation and sensibilities of parties concerned; 5) extent to which such conduct offends a public sense of justice and propriety; and 6) proportion that the punitive damage award bears to the compensatory damage award.[146] Interestingly, the court seemed only to rely upon the comparison of actual damages to punitive damages in concluding that the eight million dollar ($8,000,000) award was excessive.[147] Even though the court acknowledged that MONY had net assets in excess of eight billion dollars, the factor requiring consideration of the defendant's financial worth was apparently given little or no attention.[148] Likewise, the culpability of the defendant obviously warranted little consideration, as MONY clearly knew of discrepancies within their records yet they failed to reasonably investigate Dr. Wesson's claim.[149] In dissent, Justice Anderson ruled that such factors as culpability, net worth, and deterrence in fact justified the punitive award granted by the jury below.[150] Ultimately, *Mutual Life* seems only to define a set of factors to consider when making a punitive damage award while giving little or no guidance as to the importance of each factor.

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[136] *Mutual Life Ins. Co.*, 517 So. 2d at 532. The amount of the punitive damage award should be sufficient to discourage similar conduct in the future. *See* Standard Life Co. v. Veal, 354 So. 2d 239, 248 (Miss. 1977)(award should deter defendant from similar conduct in future).

[137] *Mutual Life Ins. Co.*, 517 So. 2d at 532. The punitive award should deter other similarly situated individuals from engaging in like conduct. *See* Reserve Life Ins. Co. v. McGee, 444 So. 2d 803, 808 (Miss. 1983)(punitive award should discourage similar conduct); T.C.L., Inc. v. LaCoste, 431 So. 2d 918, 923 (Miss. 1983)(same).

[138] *Mutual Life Ins. Co.*, 517 So. 2d at 532. *See also* Collins v. Black, 380 So. 2d 241, 244 (Miss. 1980)(financial ability to satisfy punitive award is to be considered); Allen v. Ritter, 235 So. 2d 253, 256 (Miss. 1970)(same).

[139] *See infra* notes 145-52 and accompanying text.

[140] *Mutual Life Ins. Co.*, 517 So. 2d at 532. Recognition of this principle would seem to demand an affirmation of the jury verdict absent exceptional circumstances. However, the Mississippi Supreme Court did not seem to give much deference to the jury verdict even though the court recognized the defendant's culpability. *Id.* at 528-29; *see infra* note 152 and accompanying text.

[141] *Mutual Life Ins. Co.*, 517 So. 2d at 532.

[142] *Id.* Although the court never stated which of the three exceptions was applicable to the case at bar, apparently the award was deemed unreasonable since the court noted that the award was excessive. *Id*; *see* Fowler Butane Gas Co. v. Varner, 244 Miss. 130, 151, 141 So. 2d 226, 233 (1962)(punitive damage award should operate as punishment for wrongdoer); Hines v. Imperial Naval Stores, 101 Miss. 802, 806, 58 So. 650, 651 (1912)(same).

[143] *See supra* notes 137-39 and accompanying text.

[144] 714 S.W.2d 329 (Tex. Civ. App. 1986).

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[145] *Mutual Life Ins. Co.*, 517 So. 2d at 532-33. *Ford Motor* involved a wrongful death claim resulting from the explosion of a gas tank on a Ford automobile. *Id.* at 532. The punitive damage award was remitted from $100,000,000 to $20,000,000. *Id.* Also, the deceased was a child thus giving rise to many sympathy factors. *Id.*

[146] *Mutual Life Ins. Co.*, 517 So. 2d at 532-33.

[147] *Id.* at 533. Actual damages were stipulated to be $87,136, the face amount of the insurance policy. In comparison, the $8,000,000 punitive damage award was approximately ninety-two times more than actual damages. *Id.*

[148] *Id.* at 533 n.4. Arguably, an $8,000,000 punitive award (one-tenth of one-percent of MONY's net assets) is not that unreasonable when considered in conjunction with MONY's total financial worth. Likewise, the $1,500,000 remittitur arguably will not be as effective as a deterrent. The court relied upon an affirmation by a California appellate court of a remittitur from $125,000,000 to $3,500,000. *See* Grimshaw v. Ford Motor Co., 119 Cal. App. 3d 757, 824, 174 Cal. Rptr. 348, 391 (1981)(reduction of punitive damage award was justified).

[149] *Mutual Life Ins. Co.*, 517 So. 2d at 528-29. The court did not discuss the culpability of MONY as it applied to the ultimate punitive damage award. However, in an earlier portion of the opinion, the court noted numerous occurrences which reflected the culpability of MONY. *Id.* Thus, it seems that one must simply guess at what subjective value each factor may be given in determining the final punitive damage award. But, one must remember the hollow statement made by the court that each factor should be considered equally. *Id.* at 532.

[150] *Id.* at 539-40 (Anderson, J., dissenting). Justice Anderson charged that the majority erred in considering proportionality instead of net worth. *Id.* at 539. Likewise, the dissent observed that on the basis of the majority's holding, a defendant could be assured that punitive damages would be less than one-percent of his net worth. *Id.*; *see* Downey Savings & Loan Assoc. v. Ohio Cas. Ins. Co., 189 Cal. App. 3d 1072, 1100, 234 Cal. Rptr. 835, 851 (1987)($5 million punitive damage award represented 1.9% of com-

B. *Definition of Actual Physical Contact*

At issue in *Southern Farm Bureau Casualty Insurance Co. v. Brewer* [151] was whether the propelling of an independent object by an automobile driven by an uninsured motorist through the windshield of an insured automobile constituted "physical contact."[152] Southern Farm Bureau contracted with Brewer to provide uninsured motorist coverage.[153] While driving one day, the Brewer's automobile was struck by a brake drum. The brake drum was propelled into the Brewer's automobile when a passing unidentified truck struck the drum as it lay in the road.[154] Since the passing unidentified truck did not come into contact with the Brewer's automobile, the question was whether the uninsured motorist coverage which required "physical contact" was applicable.[155]

The Mississippi Supreme Court noted that pursuant to the language of the insurance policy and statutory language,[156] physical contact was required before liability attached under the insurance policy.[157] Relying upon *Springer v. GEICO*,[158] the court concluded that

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pany's net worth); Ford Motor Co. v. Durrill, 714 S.W. 2d 329, 346 (Tex. App. 1986)($10 million punitive damage award). Finally, Justice Anderson referred to Toyota Motor Co., Ltd. v. Sanford, 375 So. 2d 1036, 1037 (Miss. 1979) in noting that a jury verdict should not be disturbed because it "seems too high, or seems too low." *Mutual Life Ins. Co.*, 517 So. 2d at 540.

[151] 507 So. 2d 369 (Miss. 1987).

[152] *Id.* at 370.

[153] *Id.* The insurance policy was issued to Stephen Blackwell, Brewer's husband. The policy provided uninsured motorist coverage of $10,000 per person. *Id.*

[154] *Id.* At the time of the accident, Jessie Brewer was driving and was a covered person under the insurance policy. *Id.* The driver of the truck did not stop, and it was stipulated that such driver was the sole and proximate cause of the accident. *Id.* The brake drum crashed through the windshield and struck Brewer in the face. *Id.*

[155] *Id.* Obviously, Southern Farm Bureau argued that physical contact required that the two vehicles involved in the accident come in "direct" contact with each other. *Id.* at 370-71.

[156] *Id.* at 370. MISS. CODE ANN. § 83-11-103(c)(v)(Supp. 1987) requires that two vehicles have "actual physical contact" before the Uninsured Motorist statutes would apply. MISS. CODE ANN. § 83-11-103(c)(v)(Supp. 1987) Thus, the construction of "physical contact" by the court in *Southern Farm Bureau* will apply to insurance policies as well as suits brought pursuant to the Mississippi statutes.

[157] *Southern Farm Bureau*, 507 So. 2d at 370. The insurance policy required that any damage be the result of "physical contact" between the uninsured automobile and

the physical contact requirement could be satisfied by either direct or indirect contact.[159] However, any indirect contact must occur as the result of "an unbroken chain of events" initiated by the uninsured or unidentified automobile.[160] This case may be distinguishable from other physical contact cases in that damages were stipulated and hence, no fraud claim existed.[161]

VI. Trusts

In 1987, the Mississippi Supreme Court addressed issues concerning charitable trusts[162] and discretionary trusts.[163] In *Tinnin v. First United Bank of Mississippi*[164], the court confronted the effectiveness of a racially discriminatory clause incorporated within a testamentary charitable trust.[165] Allen R. Hobgood executed a holographic will prior to his death on January 31, 1968.[166] The will of Mr. Hobgood contained the following provision:

> After the death of my mother, my trustees shall, in their discretion, make loans to students of a state college or university owned and operated by the State of Mississippi, who are found worthy and *who are of the Caucassion [sic] race and to*

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the insured's automobile. *Id.*

[158] 311 So. 2d 36 (La. App. 1975).

[159] *Southern Farm Bureau*, 507 So. 2d at 372. The court stated that previous Mississippi cases similar to the case at bar were distinguishable. *See* Aetna Cas. & Surety Co. v. Head, 240 So. 2d 280 (Miss. 1970) *and* George v. Mississippi Farm Bureau Mutual Ins. Co., 250 Miss. 847, 168 So. 2d 530 (1964)(*Head* wrongfully relied on *George* as holding in *George* was premised on specific contractual language); State Farm Mutual Automobile Ins. Co. v. Johnson, 242 Miss. 38, 42, 133 So. 2d 288, 290 (1961)(board propelled from automobile tire which struck insured yielded compensable injuries).

[160] *Southern Farm Bureau*, 507 So. 2d at 372. In essence, there must not be some intervening cause of the damages. *See also* Barfield v. Insurance Co. of North America, 443 S.W.2d 482, 486 Tenn. (1968)(stone hurled from one vehicle into second vehicle constitutes physical contact; Tennessee statute identical to Mississippi statute being construed); Johnson v. State Farm Mutual Automobile Ins. Co., 424 P.2d 648, 650 (Wash. 1967)(indirect physical contact will suffice).

[161] *Southern Farm Bureau*, 507 So. 2d at 372. The court noted that physical contact requirements were necessary to prevent fraudulent claims. *Id.*

[162] Tinnin v. First United Bank of Mississippi, 502 So. 2d 659 (Miss. 1987).

[163] Gulf National Bank v. Sturtevant, 511 So. 2d 436 (Miss. 1987).

[164] 502 So. 2d 659 (Miss. 1987).

[165] *Id.* at 661; *see infra* note 168 and accompanying text.

[166] *Tinnin*, 502 So. 2d at 661. Hobgood's will was prepared in December of 1962. A codicil was executed on April 22, 1967; however, the discriminatory clause at issue herein was readopted. Of particular importance was the fact that the will left no benefits to any relative other than Hobgood's mother. *Id.* at 662.

none other. (emphasis added).[167]

Allan Hobgood's mother predeceased him and hence, the racially discriminatory trust was apparently ripe for enforcement.[168] Subsequently, First United Bank of Mississippi [hereinafter Bank] was appointed trustee and proceeded to implement the trust without regard to "race, color or creed."[169]

Approximately fifteen years after the death of Allan Hobgood, the racially discriminatory clause incorporated in the trust was discovered by Hobgood's alleged heirs at law. The four plaintiffs in this litigation were the children of Hobgood's sole heir at law, Lucille Hobgood Tinnin, an aunt of the half blood.[170] Prior to the trial, the parties stipulated that in the event the trust was found inoperative, the plaintiffs in this lawsuit were in fact the proper owners of the trust assets.[171] However, the chancery court below upheld the trust reasoning that ". . . the unlawful racial restriction, being only incidental, not integral, to the primary objective of the testator, must be set aside to enable the testator's principal purpose to be carried out."[172]

At the outset, the Mississippi Supreme Court stated that enforcement of the racially discriminatory clause contained within Hobgood's will was not an available option.[173] Hence, the ultimate question became whether the court could modify the discriminatory clause by way of the *cy pres* doctrine or whether the trust must fail because such clause was an integral part of the testator's will.[174] Before examining the applicability of the *cy pres* doctrine to Hobgood's will, the court noted the importance of ascertaining and effectuating the intent of a testator.[175]

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[167] *Id.* at 661. Additionally, the trust instrument defined the terms under which the loans were to be made. For example, interest rates, repayment schedules, and amounts were mentioned. *Id.*

[168] *Id.* at 662. Hobgood's will initially provided that the funds of the trust were to be used for the sole benefit of his mother. However, this provision became unimportant as Hobgood's mother predeceased him by one month. *Id.* The court noted that the early death of Hobgood's mother was a factor to consider in ascertaining Hobgood's intent in regard to possible alteration of his will. *Id.* at 669.

[169] *Id.* at 662. When First United Bank was appointed as trustee by the court, no mention was made of the discriminatory clause. Subsequently, the Bank secured tax exempt status for the trust and pledged to implement the trust on a non-discriminatory basis. Furthermore, a court order dated August 4, 1970, apparently construed Hobgood's will; however, again no mention was made of the discriminatory clause. Likewise, the Bank failed to disclose its non-discriminatory policy to the court. *Id.*

[170] *Id.* Allan Hobgood was an only child and was single at death. The plaintiffs herein were born unto Eddie Earl Tinnin and Lucille Hobgood Tinnin. Both Eddie and Lucille Tinnin predeceased Allan Hobgood and thus, the children were rightful heirs by way of representation. Allan Hobgood also had first cousins of the full blood but under Mississippi law, Lucille Tinnin's inheritance right is superior to the cousins. *Id.* Of extreme importance to this case was the fact that nowhere in Hobgood's will was there an expressed intent to confer a benefit on the plaintiffs herein. *Id.* at 669.

[171] *Id.* at 662; *see* MISS. CODE ANN. § 91-1-1, *et seq.*, (1972)(upon lapse of devise, estate assets pass to testator's heirs at law under intestacy statutes).

[172] *Tinnin*, 506 So. 2d at 662. In essence, the chancery court believed the charitable purpose was more important to Allan Hobgood than was racial enforcement of such purpose. Hence, the trust was simply continued, absent the discriminatory provision. *Id.*

In *Tinnin*, the court relied upon *Estate of Bunch v. Heirs of Bunch*[176] to define the limitations of the *cy pres* doctrine.[177] Basically, a court must make supplementary and administrative changes in the language of the will to effectuate a testator's general charitable purpose.[178] However, the court was also careful to point out that supplementary and administrative changes could not operate to alter or defeat the testator's true intent.[179] Thus, the threshold question was whether Allan Hobgood intended the racially discriminatory clause to be merely incidental to the overall charitable purpose of the trust or whether the clause was an integral part of the testator's intent.[180] More specifically, the court stated that the ultimate question in *Tinnin* was whether the trust should continue on a non-discriminatory basis or whether the plaintiffs should be awarded the trust assets.[181] Upon reaching this issue, the court concluded that the record from the trial court below was not sufficient so as to accurately determine Hobgood's intent.[182]

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[173] *Id.* at 665-66. Enforcement of such a discriminatory clause would be against public policy. *See In re* Griffin's Will, 411 So. 2d 766, 767 (Miss. 1982)(absent violation of public policy, testator's intent must be given effect). Furthermore, a discriminatory clause may not be enforced by a state court because such enforcement would constitute state action and thus be violative of the fourteenth amendment. *See* Shelley v. Kraemer, 334 U.S. 1, 20 (1948)(state enforcement of discriminatory contract provision violates equal protection clause). Additionally, the parties agreed that the racially discriminatory clause in Hobgood's will could not be enforced. *Tinnin*, 502 So. 2d at 664-66.

[174] *Tinnin*, 502 So. 2d at 665. Thus, the answer to this question must necessarily be determined by ascertaining what the testator's intent would have been had he known the clause was not enforceable. *Id.* at 668-89.

[175] *Id.* at 663. Section 91-5-1 of the Mississippi Code gives an individual the right to control the disposition of his property upon death. MISS. CODE ANN. § 91-5-1 (1972). Thus, in order to effectuate this statutory provision, Mississippi courts must determine and enforce the true intent of a testator. *See* Deposit Guaranty National Bank v. First National Bank of Jackson, 352 So. 2d 1324, 1326-27 (Miss. 1977)("paramount and controlling consideration is to ascertain and give effect to the intention of the testator"). Therefore, in view of this well established right, a court must not arbitrarily apply the *cy pres* doctrine to promote what appears to be a fair result. *See* Estate of Bunch v. Heirs of Bunch, 485 So. 2d 284, 285 (Miss. 1986)(*cy pres* doctrine used only to enforce testator's dominant intent); *see also* MISS. CODE ANN. §§ 91-1-1, *et seq.* (1972)(if intent of testator is not ascertainable or not enforceable, then descent, distribution statutes control passage of property).

[176] 485 So. 2d 284 (Miss. 1986).

[177] *Tinnin*, 502 So. 2d at 663-65.

[178] *Estate of Bunch*, 485 So. 2d at 286. The danger in allowing such changes is that the intent of the testator may be altered or defeated by an independent third party. However, this danger is lessened by the fact that changes may be made only in provisions of the will which are "incidental" to the testator's overall purpose. *Tinnin*, 502 So. 2d at 664; *see also infra* note 180 and accompanying text.

[179] *Tinnin*, 502 So. 2d at 664. Again, the right of a decedent to direct, upon death,

Even though the ultimate issue was not decided, the court noted several cases[183] and factors to consider when ascertaining a testator's intent and the potential applicability of the *cy pres* doctrine. For example, the court stated that extrinsic evidence was to be used in conjunction with documentary evidence in determining the ultimate issue of intent.[184] In conclusion, the overall effect of *Tinnin* seems to be that the application of the *cy pres* doctrine, in the context of testamentary clauses which are against public policy, will be determined on a case by case basis so as to advance the true intent of the testator.

A second case addressed by the Mississippi Supreme Court con-

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the distribution of his estate is to be given primary consideration. *Id.* at 663; *see also supra* note 176.

[180] *Tinnin*, 502 So. 2d at 668-70. The court noted that it was not sufficient to merely attach a label to a given provision of a will; but, one must closely analyze all the facts and circumstances so as to determine which of two probably unintended results would be most consistent with the expressed intent of the testator. *Id.* at 669.

[181] *Id.* at 667-68. Even though these two alternatives were clearly unintended, the court concluded that Hobgood's will should be construed, if possible, in a manner consistent with the general purposes of the testator. *Id.* at 669; *see also* Mississippi School for Blind v. Armstrong, 216 Miss. 348, 356-57, 62 So. 2d 369, 371-72 (1953)(alternative dispositions should effectuate testator's general intentions as defined by reconstructed will).

[182] *Tinnin*, 506 So. 2d at 669.

[183] *Compare* Pennsylvania v. Brown, 392 F.2d 120, 125 (3rd Cir. 1968)(*cy pres* doctrine applied to alter testamentary trust originally established to benefit poor male white orphan children) *and* United States v. Hughes Memorial Home, 396 F. Supp. 544, 547 n.2 (W.D. Va. 1975)(clause which established orphanage "for the white children . . ." was incidental to testator's primary purpose), *with* Evan v. Newton, 148 S.E. 2d 329, 330-31 (Ga. 1966), *aff'd sub nom*, Evans v. Abney, 396 U.S. 435 (1970)(trust providing funds to establish "for whites only" park could not be salvaged simply by removing racial restrictions) *and* La Fond v. City of Detroit, 98 N.W.2d 530, 532 (Mich. 1959)(trust established to create "playfield for white children" could not be altered by *cy pres* doctrine).

[184] *Tinnin*, 502 So. 2d at 669-70. Extrinsic evidence would be helpful in determining the relationship between Hobgood and the plaintiffs as well as ascertaining Hobgood's desire to provide young people with means of securing an education. *Id.*

cerning trusts was *Gulf National Bank v. Sturtevant.*[185] In *Gulf National*, a deceased mother had established two trusts for the benefit of her only son. One of these trusts provided that the son should receive a monthly "sum sufficient for his maintenance, comfort and medical expenses."[186] The second trust provided for payments to the son in the sole discretion of the trustee with such payments never to exceed $200.[187] Gulf National Bank, as trustee, had consistently paid the son $1,100 per month of which $400 was garnished by the IRS to satisfy a tax lien.[188] Additionally, Gulf National Bank had made no payments for the past two years from the trust which allowed for discretionary expenditures not to exceed $200.[189] Consequently, the son brought suit so as to force Gulf National Bank to increase the payments from the trusts. The lower court ordered the bank to make a lump sum payment to the son and to increase monthly payments.[190]

In *Gulf National*, the Mississippi Supreme Court noted that a trustee of a discretionary trust has a responsibility to act in a manner which furthers a settlor's obvious intent.[191] Thus, a discretionary trust clearly does not allow the trustee to ignore the terms of the instrument and act as he sees fit. In the court below, the chancellor held that the son was not living "in comfort" as the trust mandated and, therefore, the trustee was abusing his discretion.[192] The Mississippi Supreme Court agreed with the chancery court and noted that comfort was to be defined by the settlor's status in life and not on the basis of the independent whims of a trustee.[193] Concluding that the chancellor was not manifestly wrong, the court affirmed.

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[185] 511 So. 2d 936 (Miss. 1987).

[186] *Id.* at 937.

[187] *Id.*

[188] *Id.* The net effect of the payment was that the son David received only $700 per month. As noted, this amount was to provide for David's "maintenance, comfort and medical expenses." *Id.*

[189] *Id.* Gulf National Bank argued that the failure to make disbursements was authorized by the trust instrument which vested in the bank, "sole discretion" to make payments. *Id.*

[190] *Id.* This conclusion was premised on the fact that David could not live "in comfort" on $700 per month. Thus, Gulf National Bank had abused its discretionary power as trustee. *Id.*

[191] *Id.* at 937; *see, e.g.*, D'everaux Hall Orphan Asylem v. Green, 226 So. 2d 725, 731 (Miss. 1969)(actions of trustee must promote intent of settlor). However, the court noted that the judgment of the trustee was to be given much deference. *Tinnin*, 502 So. 2d at 937.

[192] *Tinnin*, 502 So. 2d at 937.

[193] *Id.* at 937-38. The sole discretion of a trustee to administer trust assets as he sees fit is limited by terms such as "comfort". *See* Martin v. Martin, 374 N.E.2d 1384, 1389-90 (Ohio 1978)(words of command such as "for education, care, comfort" yield "neither

V. Elections

The Mississippi Supreme Court in 1987 rendered five decisions which dealt with election contests, three of which are discussed textually.[194] In *Wade v. Williams*,[195] the court concluded that a ballot incapable of being tabulated by a mechanical device[196] should be examined by a special tribunal[197] so as to determine the intent of the voter.[198] Also, in *Gadd v. Thompson*,[199] the court held that for Mississippi election purposes, "the filing of a homestead exemption conclusively establishe[d] domicile . . . in the county of filing."[200] Finally, in *Billings v.*

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purely discretionary trust nor strict support trust"). Additionally, the court concluded that the meaning of "comfort" was to be defined in terms of the status occupied by the settlor when the trust was created. *Tinnin*, 502 So. 2d at 938; *see also* Blodgett v. Dulaney, 201 F.2d 589, 593 (1st Cir. 1953)(comfort to be defined by social, economic status of settlor); Kuykendall v. Proctor, 155 S.E.2d 293, 301 (N.C. 1967)(same). As the settlor, Mrs. Sturtevant, enjoyed frequent travel as well as a substantial estate with servants, the court concluded that "comfort" clearly encompassed more than was being enjoyed by David Sturtevant. *Tinnin*, 502 So. 2d at 938.

[194] For a complete review of the two cases not discussed, see McDaniel v. Beane, 515 So. 2d 949, 951 (Miss. 1987)(attorneys representing election candidate cannot file certificate required by Miss. Code Ann. § 23-15-927 (Supp. 1987)) and Middleton v. Evers, 515 So. 2d 940, 944 (Miss. 1987)(voters' conviction of crimes in other states does not disqualify them from voting in Mississippi Special Mayoral election).

[195] 517 So. 2d 573 (Miss. 1987).

[196] *See* Miss. Code Ann. §§ 23-15-501 et seq. (Supp. 1987)(ballots may be tabulated by machines such as optical mark reader). In *Wade*, several ballots had been marked in such a way that the electronic machine would not tabulate them. *Wade*, 517 So. 2d at 575. Due to such impairment, Wade contended that the ballots should not have been counted and thus, he should be declared the victor. *Id.*

[197] *See* Miss. Code Ann. § 23-15-929 (Supp. 1987)(special tribunal is to be convened to ascertain intent of voters in event of election contest). The ultimate holding in *Wade* rested on a statutory mandate that the special tribunal's findings of fact are not subject to appeal if all commissioners concurred in the result. *See id.* at § 23-15-933. In *Wade*, the court was restrained by the "manifestly wrong" standard of review and hence affirmed the special tribunal's decision. *Wade*, 517 So. 2d at 576.

[198] *Wade*, 517 So. 2d at 575-76. The problem arose in *Wade* when voters failed to mark their ballots in an appropriate manner. *Id.* at 575. Thus, voter intent had to be determined without the use of machines and the special tribunal was the appropriate forum for determining such intent. *Id.*

[199] 517 So. 2d 576 (Miss. 1987).

[200] *Id.* at 579. Jack Gadd moved to Lafayette County upon securing employment there. After the move, Mr. Gadd retained no real property within Benton County, his previous residence. In March of 1986, Mr. Gadd's wife filed for homestead exemption in Lafayette County. In May of 1987, Mr. Gadd filed qualifying papers for the District 13 House of Representatives seat, a seat not including any part of Lafayette County. *Id.* at

Hollingsworth,[201] the court affirmed the assignment of the burden of proof to the party contesting the certification of election results.[202]

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577-78. The court concluded that the homestead exemption filing, as a matter of law, established Mr. Gadd's residence in Lafayette County and hence, he was not eligible for the District 13 seat pursuant to article 4, section 41 of the Mississippi Constitution. *Id.* at 578.

[201] 517 So. 2d 568 (Miss. 1987).

[202] *Id.*; *see* Berryhill v. Smith, 380 So. 2d 1178 (Miss. 1980)(allocation of burden of proof). Additionally, the court noted that such burden of proof carried a "standard of reasonable certainty." *Billings*, 517 So. 2d at 569. *See also* Necaise v. Lott, 226 Miss. 286, 294, 83 So. 2d 837 (1955)(contestant bears heavy burden of proof in election contest).

PROPERTY

The Mississippi Supreme Court handed down thirty-two decisions concerning property law in 1987. Since the majority of these decisions followed existing Mississippi precedent, they do not merit a full discussion in the text and will be relegated to the footnotes. These cases involved adverse possession,[1] annexations,[2] certificate of title,[3] delivery of deeds,[4] easements,[5] eminent domain,[6] fraudulent conveyance,[7] homesteads,[8] leases,[9] mortgages,[10] oil and gas,[11] partition,[12] restoration of property rights,[13] right of re-entry,[14] zoning,[15] and other miscellaneous aspects of property law.[16] However, two of the decisions represent significant changes in certain areas of the law, and therefore warrant full textual discussion.

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[1] *See* Pieper v. Pontiff, 513 So. 2d 591, 594 (Miss. 1987)(title to disputed property ripened by adverse possession); Roy v. Kayser, 501 So. 2d 1110, 1112 (Miss. 1987)(chancellor erred in finding title had not vested by adverse possession; existence of fence is strongest indication of adverse possession).

[2] *See* City of Greenville v. Farmers, Inc., 513 So. 2d 932, 941-42 (Miss. 1987)(only those areas found to be unreasonable when weighed by established criteria should be denied annexation); McElhaney v. City of Horn Lake, 501 So. 2d 401, 403 (Miss. 1987)(when evidence is conflicting, great deference will be given to chancellor's finding of reasonableness).

[3] *See* Hicks v. Thomas, 516 So. 2d 1344, 1346-47 (Miss. 1987)(certainty of title is required with regard to motor vehicles; therefore, title must be transferred from rightful owner).

[4] *See* Odom v. Forbes, 500 So. 2d 997, 1001 (Miss. 1987)(evidence supported finding of no legal delivery of deed).

[5] *See* Dethlefs v. Beau Maison Dev., 511 So. 2d 112, 116 (Miss. 1987)(revocable license cannot be changed to easement absent positive assertion of right hostile to owner's; lis pendens notice is not actionable for slander of title).

[6] *See* State Highway Comm'n v. Smith, 511 So. 2d 881, 883 (Miss. 1987)(testimony regarding loss of profits was reversible error due to uncertainty and speculation of future business); State Highway Comm'n v. McDonald's, 509 So. 2d 856, 860 (Miss. 1987)(court noticed plain error because trial was premised on easement giving access when all landowner had was revocable permit); State Highway Comm'n v. Havard, 508 So. 2d 1099, 1105 (Miss. 1987)(jury award of $15,000.00 was not grossly excessive, nor did it "shock the conscience"); Lawrence v. Town of Stonewall, 503 So. 2d 260, 262 (Miss. 1987)(municipality had authority to use condemned property for additional public purpose, including recreational purpose since it did not materially interfere with original use).

[7] *See* Barbee v. Pigott, 507 So. 2d 77, 85 (Miss. 1987)(no fraudulent conveyance between husband and wife where their relationship was hostile and adverse).

[8] *See* Ward v. Ward, 517 So. 2d 571, 573 (Miss. 1987)(conveyance of homestead to third party without joinder of wife is invalid); Welborn v. Lowe, 504 So. 2d 205, 207 (Miss. 1987)(conveyance invalid due to homestead exemption).

[9] *See* Weeks v. Cal-Maine Foods, Inc., 522 So. 2d 725, 728 (Miss. 1987)(court found lessor's release of assignee from obligations under lease contract was also release of lessee-assignor's contractual obligations); Sanford v. Jackson Mall Shopping Center Co., 516 So. 2d 227, 229-30 (Miss. 1987)(summary judgment inappropriate where lease was ambiguous); Leard v. Breland, 514 So. 2d 778, 782 (Miss. 1987)(damages incurred to

I. UNDUE INFLUENCE IN THE EXECUTION OF A DEED

In *Mullins v. Ratcliff*,[17] the Mississippi Supreme Court redefined the test used to rebut a presumption of undue influence in the execution of a deed. The suit arose as a result of conveyances made to Mary

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crops by breach of lease contract measured by amount of money expended to raise crop up to point of destruction); Coggins v. Joseph, 504 So. 2d 211, 214 (Miss. 1987)(no liability was imposed on successor in title to lease to pay brokerage commissions absent express agreement to do so).

[10] *See* Haygood v. First Nat'l Bank of New Albany, 517 So. 2d 553, 556 (Miss. 1987)(lower court erred in granting summary judgment on issue of adequacy of foreclosure price since fair market value of property constituted genuine issue of fact; published notice of foreclosure sale was improper); Sweet v. Luster, 513 So. 2d 1240, 1241-42 (Miss. 1987)(grantor retained same control of property after transaction as before; therefore parol evidence should have been admitted showing parties intended mortgage, not deed).

[11] *See* Brashier v. Toney, 514 So. 2d 329, 332 (Miss. 1987)(instrument conveying oil and gas rights was ambiguous; therefore, court placed construction on deed that had been placed there by parties).

[12] *See* Davis v. Davis, 508 So. 2d 1062, 1066 (Miss. 1987)(former spouse's partition action was denied by summary judgment since she had no interest in property).

[13] *See* Martin v. Phillips, 514 So. 2d 338, 341 (Miss. 1987)(finding of detrimental reliance will bar restoration of property rights to party presumed to be dead).

[14] *See* New Orleans Great N.R.R. v. Hathorn, 503 So. 2d 1201, 1203 (Miss. 1987)(summary judgment awarding right to re-enter was inappropriate since there was factual dispute about substantial compliance with conditions of deed).

[15] *See* Saunders v. City of Jackson, 511 So. 2d 902, 907 (Miss. 1987)(court must affirm where council's decision to deny rezoning was not "arbitrary and capricious"); City of Clinton v. Conerly, 509 So. 2d 877, 884 (Miss. 1987)(amendment of city's zoning ordinance was struck down due to lack of evidence supporting such changes); Belhaven Improvement Ass'n, Inc. v. City of Jackson, 507 So. 2d 41, 47 (Miss. 1987)(association has standing to sue in rezoning matters when it alleges it will suffer injury different from general public and that it represents those adversely affected).

[16] *See* Labarre v. Gold, 520 So. 2d 1327, 1331 (Miss. 1987)(court found client and his attorney guilty of conversion of security interest in property since they had actual knowledge of such interest but failed to pay upon sale of property); Madison v. Bear Creek Water Ass'n, Inc., 510 So. 2d 800, 801 (Miss. 1987)(city prohibited from taking association's Certificate of Public Convenience and Necessity because it was financed by Farmers Home Administration); Riley Bldg. Supplies, Inc. v. First Citizens Nat'l Bank, 510 So. 2d 506, 509 (Miss. 1987)(construction lender was not liable to unperfected materialman since he owed no duty of reasonable diligence in disbursing loan proceeds to owners).

[17] 515 So. 2d 1183 (Miss. 1987).

Lewis Ratcliff from her brother, James Madison (Matt) Lewis.[18] Prior to May, 1958, when Matt went to live with Mary and her husband, Lenoir, Matt had conveyed a total of forty acres to the couple. Some seven months later on February 5, 1959, Matt filed a petition requesting that a guardianship of his estate be established due to his physical handicaps.[19] The petition was granted and Mary was named as guardian.[20] On May 16, 1966, a conveyance of the last sixty of Matt's 100 acres was made to Mary by warranty deed reserving a life estate in the grantor. This deed was executed by "Mary Lewis Ratcliff GDN."[21] A second deed making the same conveyance was executed approximately a year later, but was signed by Matt's mark.[22] A. Dee Lewis Mullins and Sarah Lewis Smith, two of Matt's sisters, charged that the deeds were invalid because of undue influence.[23] The complaint also alleged that Matt lacked the requisite mental capacity to make the deeds.[24] Mary's answer specifically denied impropriety on her part or mental incapacity on Matt's part.[25]

The chancery court held that Matt's signatures were genuine and that he in fact had the mental capacity to execute the deeds.[26] The court agreed there was a presumption of undue influence with respect to the deed executed on March 29, 1967, because a fiduciary relationship existed between Mary and Matt arising out of the guardianship.[27] However, the chancellor found the presumption was successfully rebutted.[28] As a result, A. Dee and Sarah appealed from the chancery court's findings.[29]

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[18] *Mullins*, 515 So. 2d at 1186. The first two conveyances made by warranty deed and without consideration involved 20 acres respectively. *Id.* At the time the deeds were executed, April 30, 1946, and February 14, 1950, Matt was living in the home with his parents. *Id.* There was a charge of forgery with respect to these conveyances. *Id.* However, the chancery court found the signatures to be genuine and no challenge was made to this finding on appeal. *Id.* at 1188.

[19] *Id.* at 1187. From an early age Matt suffered from a condition known as hydrocephalus which is characterized by an enlarged cranium. There was contradictory evidence on his mental ability. *Id.*

[20] *Id.* at 1186. The guardianship was created so Mary could handle Matt's business affairs, namely oil, gas, and mineral leases. The guardianship was not closed until May 6, 1968. *Id.*

[21] *Id.*

[22] *Id.* The deed of March 29, 1967, was the operative deed and superseded the 1966 deed. *Id.*

[23] *Id.* at 1188. The complaint alleged that Mary, acting as guardian, deeded to herself the land in question in both the 1966 and 1967 deeds. *Id.*

[24] *Id.*

[25] *Id.* In the alternative, she also raised the affirmative defenses of adverse possession, laches and equitable and judicial estoppel. *Id.*

[26] *Id.* Although no expert testimony was given on Matt's mental capacity, doctors' statements from hospital records were admitted. The statements, made in three separate reports, found Matt to be "reasonably intelligent," "somewhat retarded," and to have "normal speech and apparent good mental ability." *Id.* at 1187. There was also testimony from family members, neighbors and friends supporting the court's finding of mental competency. *Id.*

The Mississippi Supreme Court discussed the proper scope of review of the chancery court's decision. The court stated that the lower court's findings of fact would not be reversed, even those ultimate facts,[30] where they were supported by "substantial credible evidence in the record."[31] In other words, the court would affirm unless the trial court was "manifestly wrong."[32] The court also found that a trial judge, sitting without a jury on a question of fact, had sole authority in determining witnesses' credibility.[33] Despite these well settled principles, the court concluded that "the quantum of proof the party burdened at trial was required to produce in order to prevail" had to be considered as well.[34] Therefore, when the clear and convincing evidence burden applies,[35] the court will consider that in reviewing the record.

The first issue on appeal was whether or not the chancellor's finding that Matt was mentally competent to execute the deeds was manifestly wrong and against the weight of evidence. The appellants had the burden of proving by clear and convincing evidence that Matt was mentally incompetent.[36] After reviewing the record, the court affirmed the chancellor's finding of mental competency at the time the deeds were executed.[37]

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[27] *Id.* at 1188.

[28] *Id.*

[29] *Id.* However, no challenge was made to the finding that Matt's signatures were genuine on all three deeds. *See supra* note 18.

[30] *Mullins*, 515 So. 2d at 1189 (citing Norris v. Norris, 498 So. 2d 809, 819 (Miss. 1986); Gilchrist Mach. Co., Inc. v. Ross, 493 So. 2d 1288, 1292 (Miss. 1986); Spain v. Holland, 483 So. 2d 3182, 320 (Miss. 1986); Carr v. Carr, 480 So. 2d 1120, 1122 (Miss. 1988); Check v. Ricker, 431 So. 2d 1139, 1143 (Miss. 1983)).

[31] *Mullins*, 515 So. 2d at 1188.

[32] *Id.* at 1189. The court implied that there was a duty to affirm absent manifest error. *Id.*

[33] *Id.* The court relied on Hall v. State *ex rel.* Walker, 247 Miss. 896, 903, 187 So. 2d 781, 784 (1963). *Mullins*, 515 So. 2d at 1189.

[34] *Mullins*, 515 So. 2d at 1189.

[35] *Id.* In other words, the court looks at the evidence in light of each party's burden of proof. *Id.*

[36] *Id.* at 1190. The court, citing Richardson v. Langley, 426 So. 2d 780, 783 (Miss. 1983), and Gillis v. Smith, 114 Miss. 665, 676-677, 75 So. 451, 453 (1917), stated that A. Dee and Sarah had the burden of proving Matt's lack of mental capacity by clear and convincing evidence. *Mullins*, 515 So. 2d at 1190.

The second assignment of error was the chancellor's failure to find any undue influence exercised over Matt in the execution of the 1946 and 1950 deeds. A. Dee and Sarah argued that due to Matt's state of dependency, Mary owed him a fiduciary duty.[38] After a review of the facts in the record, the court affirmed the chancellor's findings that Mary did not owe a fiduciary duty nor did she exert undue influence over Matt in 1946 or 1950.[39]

The crux of A. Dee and Sarah's appeal lay within their third assignment of error. The issue was whether or not the chancellor's finding that Mary had overcome the presumption of undue influence in the execution of the March 29, 1967, deed was manifestly erroneous and against the overwhelming weight of the evidence.[40] The court concluded that the chancery court correctly found that a confidential relationship existed giving rise to the presumption of undue influence. The lower court correctly relied on the existence of the guardianship over Matt's estate as the major fact supporting this finding.[41] In reaching its conclusion that Mary had successful rebutted this presumption, the trial court analyzed the case under the test provided in *Murray v. Laird*.[42] The three-prong test was described by the court as follows:

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[37] *Mullins*, 515 So. 2d at 1191. The court reasoned that given the challengers' burden of proof and the evidence supporting Matt's competency there was no manifest error. *Id.*

[38] *Id.* They based their argument on Hendricks v. James, 421 So. 2d 1031 (Miss. 1982). In *Hendricks*, the court stated "whenever there is a relation between two people in which one person is in a position to exercise dominant influence upon the former, arising either from weakness of mind or body, or through trust, the law does not hesitate to characterize such a relationship as fiduciary in character." *Hendricks*, 421 So. 2d at 1041.

[39] *Mullins*, 515 So. 2d at 1192. The court reasoned that although, as stated in Murray v. Laird, 446 So. 2d 575, 578 (Miss. 1984), fiduciary duties may arise from moral, domestic, or personal relationships as well as legal ones, these duties had not arisen here. *Mullins*, 515 So. 2d at 1192. The main reason for this holding appeared to be the fact that at the time of the 1946 and 1950 deeds Matt's parents were aware of and consented to the conveyance. *Mullins*, 515 So. 2d at 1192.

[40] *Mullins*, 515 So. 2d at 1189. Since Mary did clearly owe fiduciary duties to Matt in 1967, she carried the burden of rebutting the presumption of undue influence at trial. *Id.*

[41] *Id.* at 1192; *see* Costello v. Hall, 506 So. 2d 293, 296-97 (Miss. 1987)(legal relationship may support finding that confidential relationship exists).

[42] 446 So. 2d 575 (Miss. 1984). In the *Murray* case, the court affirmed the chancellor's finding of undue influence in the execution of a deed from a father to his son. *Murray*, 446 So. 2d at 578. The court's findings that the son handled the father's business transactions; the father was in poor health; the son participated in and initiated the execution of the deed; and the father obtained no independent advice supported the

> When the circumstances give rise to a presumption of undue influence, the burden of going forward with the proof shifts to the grantee/beneficiary to prove by clear and convincing evidence:
>
> (1) good faith on part of the grantee/beneficiary;
>
> (2) grantor's full knowledge and deliberation of his actions and their consequences; and
>
> (3) advice of (a) a competent person, (b) disconnected from the grantee and (c) devoted wholly to the grantor/testator's interest.[43]

The chancellor concluded that although there were no "hard and fast rules,"[44] the third part of the test was satisfied since Matt disclosed his intention about the conveyance to a disinterested person before executing the 1967 deed and later told yet another disinterested third party that he had executed such a deed.[45]

The Mississippi Supreme Court agreed that there was confusion as to exactly what the third prong required, and further concluded that in many cases it had "been read too strictly."[46] The court then stated that a showing of "independent advice"[47] was not necessary to satisfy the third prong. The court declared that "independent consent and ac-

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conception of the deed on the grounds of undue influence. *Id.* at 578-80.

[43] *Id.* at 578.

[44] *Mullins*, 515 So. 2d at 1192.

[45] *Id.* One witness, Elaine Arnold, testified that Matt told her two years before executing the 1967 deed that he intended to repay Mary and Lenoir for taking care of him by conveying his land to them. Yet another witness, Ebbie Patt, testified that prior to Matt's death he told her that he had given Mary land because she had taken care of him. *Id.* at 1195-96.

[46] *Id.* at 1193. Meek v. Perry, 36 Miss. 190 (1858), was the seminal case which held to rebut such a presumption of undue influence the grantee/beneficiary had to show the fullest deliberation by the grantor and abundant good faith by grantee/beneficiary. *Meek*, 36 Miss. at 258-59. In Ham v. Ham, 146 Miss. 161, 110 So. 583 (1926), the court required clear and convincing evidence of good faith, full knowledge, and independent consent and action. *Ham*, 110 So. at 585. However, the *Ham* court also elaborated on the third requirement by proposing the only way it could be proven would be when the grantor acted on independent advice of a competent person devoted solely to the grantor's interest. *Ham*, 110 So. at 585.

[47] However, many cases citing *Ham* have required a showing of "independent advice." *See* Hendricks v. James, 421 So. 2d 1031, 1043-45 (Miss. 1982)(required "independent advice" in order to rebut presumption); Jones v. Singley, 242 So. 2d 430, 435 (Miss. 1970)(same); *In re* Will of Moses, 227 So. 2d 829 (Miss. 1969)(same); Wofford v. Wofford, 224 Miss. 442, 459-61, 142 So. 2d 188 (1962)(same); Watkins v. Martin, 167 Miss. 343, 147 So. 652, 654 (1933)(same).

tion"[48] was the correct and appropriate third prong of the test.[49] The court based its decision not only on the history of the state's common law with regard to this area but also on common sense. The court reasoned that the modified *Murray* test was a guide to factors to be considered but was not a hard and fast rule. The test, the court stated, was to be flexible and applied with common sense.[50]

After deciding upon the appropriate test, the court applied the modified test to the fact situation. The court concluded that Mary had satisfied the good faith,[51] full knowledge,[52] and independent consent and action[53] prongs of the test. The trial court's decision was affirmed since a rational trier of fact could have reached the same conclusion based on the quality and quantity of evidence in the record.[54] In conclusion, the court found no merit in any assignments of error and affirmed the chancellor's decision.[55]

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[48] *Ham* has also been cited for the "independent consent and action" language while omitting reference to "independent advice" portion. *See* Mansell v. Gross, 345 So. 2d 1315, 1317 (Miss. 1977)(did not require "independent advice," only "independent consent and action"); Jones v. Jones, 246 So. 2d 486, 487 (Miss. 1971)(same); Thomas v. Jolly, 251 Miss. 448, 454, 170 So. 2d 16, 20 (Miss. 1964)(same); McElveen v. McElveen, 233 Miss. 672, 677, 103 So. 2d 439, 442 (Miss. 1958)(same).

[49] *Mullins*, 515 So. 2d at 1194. This was not the first time since *Murray* that the Mississippi Supreme Court used independent consent and action as the third prong. *See* Estate of Lawler v. Weston, 451 So. 2d 739, 743 (Miss. 1984)(court declined to use independent advice as third requirement); *but see*, Matter of Launius, 507 So. 2d 27, 30 (Miss. 1987)(followed *Murray* test); Kelly v. Shoemake, 460 So. 2d 811, 819-20 (Miss. 1984)(same); Harris v. Sellers, 446 So. 2d 1012, 1014-15 (Miss. 1984)(same).

[50] *Mullins*, 515 So. 2d at 1194. The court cited portions of *Murray* in support of its conclusion that the trier of fact would have to use his or her judgment in applying these guidelines to the particular facts of each case. *Id.*

[51] *Id.* at 1195. In analyzing good faith, five factors should be considered: (a) identifying the initiating party, (b) place of execution and in whose presence, (c) consideration and fee paid, if any, and (d) whom paid, and (e) secrecy and openness of the execution. *Id.* The court found these factors supported Mary's rebuttal. *Id.*

[52] *Id.* at 1195. The court looked to *Murray* and the factors suggested to determine the grantor's knowledge. The factors are: (1) awareness of total assets and their value, (2) understanding of his natural heirs at law or by previous will and how this change would affect those, (3) whether non-relative beneficiaries would be excluded or included, and (4) knowledge of who controls his finances and business and how, and, if controlled by another, was grantor dependent and susceptible to his influence. *Mullins* 515 So. 2d at 1195.

[53] *Mullins*, 515 So. 2d at 1195-96. *See supra* note 44 and accompanying text. The court found these facts together with others in the record satisfied the independent consent and action requirement. *Id.* at 1195-96.

[54] *Id.* at 1196. *See supra* notes 31-37 and accompanying text.

[55] *Mullins*, 515 So. 2d at 1196. The court refused to adopt a rule prohibiting a guardian from acquiring his ward's property during the existence of the guardianship

The *Mullins* case should clear up any confusion with respect to the application of the third prong of the *Murray* test. It is quite apparent that the modified test is not to be strictly applied, but rather a flexible guide for the trier of fact to use. Given the nature of undue influence, no hard and fast rule would be appropriate.

II. CONSTRUCTION OF OIL AND GAS CONVEYANCE

In *Thornhill v. Systems Fuels, Inc.*,[56] the Mississippi Supreme Court reversed the chancellor's finding by a 5-4 decision and held that the grantors' reservation of the rights to bonuses and delay rentals as to present or future leases did not so change the character of the mineral deed as to make it a royalty conveyance.[57] On May 14, 1945, Hardy and Josephine McLeod executed a mineral deed to C.L. Thornhill conveying an undivided one-half interest in the minerals to a portion of land in Jefferson Davis County.[58] The instrument was a standard "Form R-101 Mineral Right and Royalty Transfer" with the following typed provisions: "It is the intention of the granters to convey, and they do hereby convey, twenty (20) full mineral acres of land of said tract. Non-participating as to present or future lease rentals or bonuses."[59] Four years after the conveyance, Thornhill filed an application for ad valorem tax exemption on this acquired mineral interest labeling it "½ Royalty."[60] Over thirty years later, when production became apparent on the land in question, Thornhill brought suit claiming the 1945 deed conveyed to him an undivided one-half mineral interest in all minerals in place subject only to the grantors' reservation of all bonuses and delay rentals.[61] The chancellor, relying on *Harris v. Grif-*

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without a court's consent. *Id.*

[56] 523 So. 2d 983 (Miss. 1988)(modified on rehearing by overruling Harris v. Griffith, 210 So. 2d 629 (Miss. 1968) to extent that it conflicts with instant case).

[57] *Thornhill*, 523 So. 2d at 986. The court cited HEMINGWAY, LAW OF OIL AND GAS § 2.7 (2d ed. 1983):

> In probably no other area of oil and gas law, than in cases involving the mineral-royalty distinction, can examples be found of courts, on behalf of befuddled litigants, benevolently and improperly granting reformation in the guise of a judgment for title.

Thornhill, 523 So. 2d at 986.

[58] *Thornhill*, 523 So. 2d at 984. The legal description of such land is Northwest Quarter of the Southwest Quarter (NW¼ SW¼) of Section 30, Township 6 North, Range 17 West, in Jefferson Davis County. *Id.*

[59] *Id.* at 984.

[60] *Id.*

[61] *Id.* at 984-85.

fith,[62] found the conveyance was a non-participating royalty interest. Thornhill appealed.

In reversing, the supreme court held that the facts surrounding the McLeods' conveyance were distinguishable from those in *Harris*.[63] In *Harris*, the Mississippi Supreme Court construed a similar instrument as a conveyance of a royalty interest because it had undergone more changes since a paragraph was deleted[64] and because there were elements of estoppel against the parties claiming to own the mineral interest.[65] The court in the present case stated that *Harris* was the exception rather than the rule.[66] The court reasoned that the rule is more accurately stated that the entire instrument controls rather than particular words, as in *Mounger v. Pittman*,[67] where the court listed the characteristics of the two respective interests:

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[62] 210 So. 2d 629 (Miss. 1968). *Harris* involved a similar conveyance which was construed as a non-participating royalty interest as opposed to a mineral interest in the minerals in place. *Harris*, 210 So. 2d at 635.

[63] *Thornhill*, 523 So. 2d at 989. Although the court distinguished the case on its facts, there are striking similarities. For example, in *Harris*, the Griffiths executed a mineral conveyance on a "Form R-101" just as the McLeods did. *Harris*, 210 So. 2d at 631. Typed on the form were two sentences similar to those typed on the McLeods' conveyance; "It is the intention of the grantors herein to convey 64-¾ full mineral acres. This instrument is to be non-participating both as to bonuses and lease rentals." *Harris*, 210 So. 2d at 631. However, there were additional changes to the deed in the *Harris* case. A portion of the title and the last printed paragraph were struck out. *Harris*, 210 So. 2d at 634-35.

[64] *Harris*, 210 So. 2d at 636.

[65] *Id.* The court, in discussing the factors which were pertinent to the parties' practical construction of the instrument, stated "These include Payne's *experience and knowledge as an oil and gas investor*, Carl F. Griffith's *lack of experience and education*,the numerous changes in a printed document of known effect, and *the time and long period of delay by appellants before asserting any claim* to the executive right." *Id.* (emphasis added).

[66] '*Thornhill*, 523 So. 2d at 991. In an attempt to restrict *Harris*' holding, the court reviewed several cases that supported their construction of the *Thornhill* deed as a mineral estate conveyance. *Id.* at 986-91. The court reasoned that it is "well settled" that rights to bonuses and delay rentals could be separated without changing the conveyance to a royalty interest only. *Id.*

Other cases addressing similar issues have been decided by the Mississippi Supreme Court. The case of Ford v. Jones, 226 Miss. 716, 85 So. 2d 215 (1956), involved a conveyance similar to the one in question. The conveyance was made on a "Form R-101" mineral deed with two additional paragraphs typed in reserving to the grantor the rights to delay rentals on an existing lease. The court held the grantee acquired an interest in minerals in place, except for delay rents due on the existing lease. *Ford*, 266 Miss. at 281, 85 So. 2d at 218. In Westbrook v. Ball, 222 Miss. 788, 77 So. 2d 274 (1955), the grantor reserved to himself a mineral estate while the grantee received only the right to bonuses and delay rentals. *Westbrook*, 222 Miss. at 790-91, 77 So. 2d at 275.

[67] 235 Miss. 85, 108 So. 2d 565 (1959). The *Mounger* court construed the instrument

> The distinguishing characteristics of a nonparticipating royalty interest are: (1) Such production is not chargeable with any of the costs of discovery and production; (2) the owner has no right to do any act or thing to discover and produce the oil and gas; (3) the owner has no right to grant leases; and (4) the owner has no right to receive bonuses or delay rentals. Conversely, the distinguishing characteristics of an interest in minerals in place are: (1) Such interest is not free of costs of discovery and production; (2) the owner has the right to do any and all acts necessary to discover and produce oil and gas; (3) the owner has the right to grant leases; and (4) the owner has the right to receive bonuses and delay rentals.[68]

The court applied the conventional rules of construction[69] and found the McLeods had conveyed an undivided one-half interest in all the minerals, but retained the right to bonuses and delay rentals.[70] Hence, the court reversed the chancery court decision and rendered judgment for Thornhill.

Justice Dan Lee, joined by Chief Justice Walker, Justice Roy Noble Lee, and Justice Griffin, articulated a strong dissent.[71] The dissent argued that the *Harris* case should have controlled since the facts were so similar.[72] In fact, the dissent argued there was greater injustice in the present case than in *Harris*.[73] Not only was there great delay in

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to be a reservation of mineral interest in place. *Mounger* 235 Miss. at 86, 108 So. 2d at 566.

[68] *Id.* at 86-87, 108 So. 2d at 566.

[69] *Thornhill*, 523 So. 2d at 988 n.2. The court listed the rules of construction as follows:

> (1) In a deed where there are two repugnant clauses, the first must prevail, and (2) an attempted reservation is voided when repugnant to the granting clause, (3) these two rules shall not apply where the intent of the parties is plain. Also, when contractual provisions could not be reconciled, if part of the contract is in writing and part printed, the written part will prevail. Finally, it is the duty of the court to construe an instrument as written.

Id.

[70] *Id.*, at 992.

[71] *Id.* at 994 (Dan Lee, J., dissenting).

[72] *Id.* at 996-97 (Dan Lee., J., dissenting).

[73] *Id.* at 994 (Dan Lee, J., dissenting). The injustice in the *Harris* case arose not only because of the delay but also because of the differences in experience and knowledge of the parties. *Harris*, 210 So. 2d at 636. Apparently, the key factor giving rise to the estoppel was the Griffiths had borne the burden of production costs and attorneys fees. It was not until a commercial well was produced that the complainants argued they had a min-

asserting the claim, but the McLeods were uneducated farmers who signed the conveyance with "X's", while Thornhill, on the other hand, was fairly sophisticated in oil and gas leases.[74] Therefore, aside from the provisions stricken from the *Harris* conveyance, the dissent found the cases remarkably similar. Justice Dan Lee argued, rather persuasively, that the majority's decision further blurred the legal distinctions between a royalty deed and a mineral deed.[75]

The dissent further reasoned that the majority had abused the standard of review given to a chancellor's decision once his findings of fact have been made.[76] The dissent contended there was "substantial credible evidence" in support of the chancellor's findings, and there was no "manifest error" in his decision.[77] The dissent relied upon *Dunaway v. Busbin*,[78] wherein the court stated:

> We have repeatedly refused to reverse a chancery court's finding of fact where there is any substantial credible evidence which supports it . . . . Put otherwise, the chancery court's findings must be allowed to stand unless manifest error is present and apparent.[79]

Justice Dan Lee, concluding that the chancellor correctly applied the case of *Harris v. Griffith* and that his findings could not be said to be manifestly wrong,[80] stated that he would have affirmed.[81]

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eral interest of the minerals in place. *Id.*

[74] *Thornhill*, 523 So. 2d at 998 (Dan Lee, J., dissenting). In *Harris*, the Mississippi Supreme Court found this difference in the education and experience of the parties an important factor in the construction of the conveyance. *Harris*, 210 So. 2d at 636.

[75] *Thornhill*, 523 So. 2d at 998 (Dan Lee, J., dissenting). Justice Dan Lee suggested the majority had, through their decision, "fashioned a legal theory that has little practical meaning, except to open the door for title busters and oil sharks to feast upon the unsuspecting people unversed in the legal niceties of theories and terminology." *Id.* at 1000.

[76] *Id.* at 999 (Dan Lee, J., dissenting).The dissent cited several cases articulating the appropriate standard of review including Culbreath v. Johnson, 427 So. 2d 705, 707 (Miss. 1983)(evidence and inferences reasonably drawn from it in support of decree must be accepted); Blakeney v. Blakeney, 244 So. 2d 3, 4 (Miss. 1971)(same); and Richard v. Riley, 355 So. 2d 667, 668 (Miss. 1978)(cannot disturb chancellor's finding of facts absent manifest error). *Thornhill*, 523 So. 2d at 999-1000.

[77] *Thornhill*, 523 So. 2d at 1000 (Dan Lee, J., dissenting).

[78] 498 So. 2d 1218 (Miss. 1986).

[79] *Thornhill*, 523 So. 2d at 999 (Dan Lee, J., dissenting)(citing Dunaway v. Busbin, 498 So. 2d 1218, 1220).

[80] *Thornhill*, 523 So. 2d at 994-1000.

[81] *Id.* at 1000.

TORTS

In 1987, the Mississippi Supreme Court decided a number of tort cases, three of which warrant commentary. Other cases adjudicated addressed issues of damages,[1] professional malpractice,[2] defamation,[3] premises liability,[4] negligence,[5] products liability,[6] wrongful death,[7] re-

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[1] Seaboard Systems Railroad, Inc. v. Cantrell, 520 So. 2d 479, 485 (Miss. 1987) (failure to give instruction that award was not subject to taxation was reversible error); James v. Jackson, 514 So. 2d 1224, 1227 (Miss. 1987)(order of additur was reasonable exercise of discretion in response to inadequate damage award); Hutchins v. Page Contractors, Inc., 513 So. 2d 944, 945-46 (Miss. 1987)(appropriateness of jury view for determination of liability and damages is within discretion of trial judge); Stratton v. Webb, 513 So. 2d 587, 591 (Miss. 1987)(remittitur proper as judge considered all relevant evidence including aggravating effect of subsequent injuries); West v. Plastifax, Inc., 505 So. 2d 1026, 1029 (Miss. 1987)(exclusive remedy provisions of Worker's Compensation Act bar spouse's claim for loss of consortium); City of Jackson V. Keane, 502 So. 2d 1185, 1188 (Miss. 1987)(landowner can recover reasonable and necessary expenses incurred in attempt to prevent future damages); McIntosh v. Deas, 501 So. 2d 367, 369 (Miss. 1987)(judge must find jury verdict evinces bias, passion, and prejudice, or was contrary to overwhelming weight of evidence before usurping jury's damages decision).

[2] Phillips v. Hull, 516 So. 2d 488, 494 (Miss. 1987)(issues relating to informed consent are not beyond common knowledge of laymen; thus, expert testimony is not required of plaintiff on consideration of summary judgement motion); Bass v. Montgomery, 515 So. 2d 1172, 1175 (Miss. 1987)(defendant's favorable legal malpractice jury verdict was supported by evidence which was not tainted with bias, prejudice, or passion); Ladner v. Campbell, 515 So. 2d 882, 889-90 (Miss. 1987)(expert medical testimony was erroneously excluded because knowledge criteria applied was previous statewide standard of care instead of nationwide standard of care); Burnham v. Tabb, 508 So. 2d 1072, 1077 (Miss. 1987)(jury determination of proximate cause was rationally based on evidence adduced at trial); Kilgore v. Barnes, 508 So. 2d 1042, 1045 (Miss. 1987)(limitations period in medical malpractice action does not begin to run until date negligent act shall, or with reasonable diligence, might have been first discovered); Brown v. Mladinco, 504 So. 2d 1201, 1203 (Miss. 1987)(medical malpractice action); Hickox v. Holleman, 502 So. 2d 626, 633 (Miss. 1987)(plaintiff must show that but for attorney's negligence, success would have ensued on underlying claim).

[3] Baugh v. Baugh, 512 So. 2d 1283, 1285 (Miss. 1987)(statements as to defendant's medical condition did not impute his behavior as criminally fraudulent; thus, they were not slanderous per se); Chatham v. Gulf Publishing Co., Inc., 502 So. 2d 647, 650 (Miss. 1987)(articles did not contain language which clearly and unmistakably, without use of innuendo, speculation, or inference, injured plaintiff's reputation).

[4] Noel's Auto Electric Service, Inc. v. Jones, 516 So. 2d 503, 504-05 (Miss. 1987)(under prior rules of evidence, lay opinion testimony on ultimate issue is merely harmless error); Elder v. Sears, Roebuck & Co., 516 So. 2d 231, 236 (Miss. 1987)(local catalogue merchant was under sufficient control of Sears to find agency relationship which resulted in Sears being vicariously liable); Kroger, Inc. v. Ware, 512 So. 2d 1281,

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1282 (Miss. 1987)(no liability for injuries where condition causing fall was known and obvious to plaintiff); Carpenter v. Stop-N-Go Markets, Inc., 512 So. 2d 708, 709 (Miss. 1987)(convenience store owner does not have duty to erect barrier at storefront in order to prevent vehicular injuries to patrons inside); Davis v. Singing River Elec. Power Ass'n, 501 So. 2d 1128, 1130 (Miss. 1987)(no liability for injuries where dangerous conditions were obvious and should have been known by plaintiff); Joseph v. Tennessee Partners, Inc., 501 So. 2d 371, 376 (Miss. 1987)(liability of owner or occupier of real estate depends upon control of property).

[5] Wactor v. John H. Moon & Sons, Inc., 516 So. 2d 1364, 1367 (Miss. 1987)(although trial experts' testimony was based on view of accident site after repair, it was admissible because experts based their testimony on conditions that existed before repair was made); Read v. Southern Pine Elec. Power Ass'n, 515 So. 2d 916, 919 (Miss. 1987) (power companies under highest duty of care in distributing electricity); Sugg v. Sanderson, 515 So. 2d 909, 911 (Miss. 1987)(proper jury instruction requires support by some credible evidence); Williams v. Dixie Elec. Power Ass'n, 514 So. 2d 332, 336-37 (Miss. 1987)(failure to tender requested discoverable evidence to adversary prohibited its admission at trial); White v. Miller, 513 So. 2d 600, 602-03 (Miss. 1987)(plaintiff was entitled to peremptory instruction that defendant was liable for causing rear-end collision); City of New Albany v. Barkley, 510 So. 2d 805, 807 (Miss. 1987)(city's failure to maintain drainage culverts was not proximate cause of business' flooding during extraordinary rain storm); Blackmon v. Payne, 510 So. 2d 483, 487 (Miss. 1987)(jury instruction was erroneous because it failed to incorporate comparative negligence principles in proximate cause determination); Bryant v. Alpha Entertainment Corp., 508 So. 2d 1094, 1097 (Miss. 1987)(violation of statute which prohibits sale of alcohol to people under 18 years of age was negligence per se); Dale v. Bridges, 507 So. 2d 375, 377-78 (Miss. 1987)(failure to stop at railroad crossing when approaching train was plainly visible was prima facia evidence of negligence); Brown v. Williams, 504 So. 2d 1188, 1194 (Miss. 1987)(general contractor enjoyed immunity from claim of subcontractor's employee because MISS. CODE ANN. § 71-2-7 (1972) imposed duty to have worker's compensation coverage); Jones v. Hatchett, 504 So. 2d 198, 202 (Miss. 1987)(party must supplement discovery requests to reveal identity and expected testimony of experts not stated in original discovery responses); Collins v. Ringwald, 502 So. 2d 677, 678-79 (Miss. 1987)(whether automobile proceeded cautiously through yellow traffic light was jury question).

[6] Smith v. Fluor Corp., 514 So. 2d 1227, 1230-31 (Miss. 1987)(heater exchanger was found to be improvement to real property thus causing application of MISS. CODE ANN. § 15-1-41 (1972) and barring claim); Detroit Marine Eng'g v. McRee, 510 So. 2d 462, 465 (Miss. 1987)(no product misuse for utilizing higher horsepower motor on boat officially rated for use at lower horseposer level); B.F. Goodrich, Inc. v. Taylor, 509 So. 2d 895, 903 (Miss. 1987)(evidence supported jury finding that injury-producing tire was defective when it left manufacturer).

[7] Mitcham v. Illinois Cent. Gulf R.R. Co., 515 So. 2d 852, 854 (Miss. 1987)(motorist must stop at railroad crossing if conditions imposed by MISS. CODE ANN. § 77-9-249 (1972) occur); Bland v. Briggs, 512 So. 2d 894, 896 (Miss. 1987)(motorist is imposed with higher duty to expect unexpected and unusual from nearby children and must operate vehicle accordingly); Estate of Morris v. W.E. Blain & Sons, Inc., 511 So. 945, 949-50 (Miss. 1987)(subcontractor working under same prime contractor as another does not enjoy workers' compensation exclusive remedy immunity); Estate of Faggard v. Magnolia Elec. Power Ass'n, 511 So. 2d 939, 943-44 (Miss. 1987)(electricity supplier has no control and no commensurate duties for wiring running beyond original pole meter connection

spondeat superior,[8] conversion,[9] fraudulent misrepresentation,[10] malicious prosecution,[11] and false imprisonment.[12]

I. Independent Auditor Liability.

In *Touche Ross & Co. v. Commercial Union Insurance Co.*,[13] the Mississippi Supreme Court adopted the "reasonably foreseeable" standard in determining to whom an independent auditor is liable for negligently prepared financial reports.[14] Relying upon the standard expressed in *H. Rosenblum, Inc., v. Adler*,[15] the court held that an independent auditor is liable to reasonably foreseeable users of the audit, who, after requesting and receiving the statements from the audited entity for a proper business purpose, detrimentally rely on the information and suffer losses proximately caused by the auditor's negligence.[16]

The litigation in *Touche Ross* arose as a result of the insolvency of

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toward private property); Hughes v. Tupelo Oil Co., 510 So. 2d 502, 504 (Miss. 1987)(patrol officer's testimony that no traffic citation was issued was inadmissible as it constituted unhelpful opinion on ultimate issue).

[8] Marter v. Scott, 514 So. 2d 1240, 1242-43 (Miss. 1987)(vacationing employee who was acting as "good samaritan" toward fellow employee was not acting within course and scope of employment).

[9] Walker v. Brown, 501 So. 2d 358, 361 (Miss. 1987)(intent to exercise dominion and control over tractor trailor inconsistent with owner's rights constituted conversion).

[10] Rankin v. Brokman, 502 So. 2d 644, 646 (Miss. 1987)(requisite misrepresentation was not made when plaintiff signed obvious warranty deed and bill of sale and buyer did not represent them to be anything else).

[11] 'Mississippi Road Supply Co. v. Zurich-American Ins. Co., 501 So. 2d 412, 414-15 (Miss. 1987)(summary judgment in malicious prosecution action was inappropriate as disputed material facts existed).

[12] Thornhill v. Wilson, 504 So. 2d 1205, 1209 (Miss. 1987)(officer's detention of plaintiff was reasonable and lawful).

[13] 514 So. 2d 315 (Miss. 1987).

[14] *Id.* at 322.

[15] 93 N.J. 324, 461 A.2d 138 (1983). In *H. Rosenblum*, the plaintiffs used negligently prepared financial statements when accepting stock as payment for the sale of their business. *Id.* at 153. Addressing their claim, the court explained that an auditor had a duty to all reasonably foreseeable users of information who relied upon the statements pursuant to proper business purposes. *Id.* Moreover, the users must have requested and received the information from the audited entity. *Id. See also* Citizens State Bank v. Timm, Schmidt & Co., 335 N.W.2d 361, 366-67 (Wis. 1983)(accounting firm liable for all foreseeable consequences of its acts). *Cf.* Continental Assurance Co. v. American Bankshares Corp., 601 F.Supp. 277, 281 (E.D. Wis. 1985)(exceptions to liability standard swallowed the rule).

[16] *Touche Ross*, 514 So. 2d at 322.

Fidelity Bank of Jackson, Mississippi.[17] After the bank failure, the Federal Deposit Insurance Corporation made a claim against Commercial Union,[18] the bank's insurer against employee fraud.[19] Commercial Union settled the FDIC's claim after investigations revealed that extensive losses[20] were caused by the fraudulent activity of Fidelity Bank's president, George S. Sanders, Jr.[21]

On May 6, 1983, Commercial Union filed suit against Touche Ross & Company claiming its losses were caused by the auditor's negligent preparation of financial statements upon which it relied when underwriting the employee fraud coverage.[22] The allegations of negligence[23] included the failure to disclose: (1) the Mississippi Department of Bank Supervision's objections to the payment of a March 20, 1977, dividend;[24] (2) the Department's June 1, 1977, letter requiring its consent prior to any future cash dividend payments or other transfers of funds to any affiliates or subsidiaries;[25] and (3) Fidelity Bank's $71,773 receivable from and $200,000 loan to Fidelity's former parent, Affiliated Investments, Inc., when Touche Ross questioned Affiliated's continued viability.[26] The jury awarded Commercial Union $1,000,000 in actual damages and $500,000 in punitive damages.[27] Touche Ross appealed, and the Mississippi Supreme Court reversed and rendered.[28] Although the trial court applied the appropriate auditor liability standard,[29] the court concluded that the criminal conduct of Fidelity Bank's president was the independent intervening cause of Commercial Union's losses.[30]

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[17] *Id.* at 315. Pursuant to MISS. CODE ANN. § 81-9-5 (1972), the State Comptroller declared the state chartered financial institution insolvent. *Touche Ross*, 514 So. 2d at 315.

[18] *Touch Ross*, 514 So. 2d at 315. The FDIC asserted that Fidelity's losses were the result of criminal fraud by its president, George S. Sanders, Jr. *Id.*

[19] *Id.* Commercial Union had issued a Bankers Blanket Bond to insure against employee fraud. *Id.*

[20] *Id.* Total losses amounted to $7,000,000; however, Commercial Union settled with the FDIC for $1,000,000. *Id.*

[21] *Id.* at 316.

[22] *Id.* Commercial Union asserted that Touche Ross violated Generally Accepted Accounting Principles (G.A.A.P.) and Generally Accepted Auditing Standards (G.A.A.S.) by failing to disclose certain information of which it was aware. Furthermore, Commericial Union stated that it would have refrained from issuing its insurance coverage if it had been appraised of these undisclosed facts. *Id.*

[23] *Id.* at 317. Commercial Union made several other allegations of negligent auditing. First, it argued that Touche Ross "grossly understated" the loan loss reserves of Fidelity Bank. *Id.* However, Touche Ross rebutted claiming that Commercial Union's figures failed to consider certain collateral and wrongly included certain loans. *Id.* Second, Commercial Union sharply criticized the treatment of an unsecured $240,000 loan to an individual with no prior credit history or audited financial statements. *Id.* at 318. Similarly, Commercial Union maintained that Touche Ross was negligent in not inquiring into a transaction where Fidelity loaned money for the purpose of stock purchases of its parent, Affiliated Investments. *Id.* Finally, Commercial Union questioned Touche Ross' treatment of a loan later found by the FDIC as "fraudulently and dishonestly made." *Id.*

[24] *Id.* at 316. Fidelity Bank paid the $275,000 dividend to Affiliated Investments although previously having only $3,907 of earnings in 1976 and a loss of $16,897 in 1975. *Id.* Michael Zito, Touche Ross' partner-in-charge, had advised that funds were available for this dividend payment. After investigation, the Mississippi Department of Bank Supervision determined that this dividend was "highly irregular, if not illegal." Likewise, an FDIC probe concluded that a number of regulations, sound banking practices, and state laws were violated including the misuse of surplus account funds. *Id.*

More importantly, however, the supreme court established a standard to determine to whom a negligent independent auditor may be liable.[31] In analyzing this issue, the court categorized and addressed the following four jurisdictional views:

1. The *Ultramares* doctrine which essentially requires privity between the auditor and user;[32]

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[25] *Id.* Pursuant to Miss. Code Ann. § 81-5-75 (1972), the state comptroller notified Fidelity that all dividend payments and transfers of funds required regulator approval. *Touche Ross*, 514 So. 2d at 316-17. However, approximately 6 months later Fidelity loaned Affiliated Investments $200,000, four days after Affiliated divested itself of the bank. Touche Ross failed to question the loan's legality and claimed it had no knowledge of the regulator approval requirement. *Id.* at 317.

[26] *Touch Ross*, 514 So. 2d at 317. Touche Ross also audited Affiliated Investments. However, it refused to offer an opinion on the firm's financial statements because of Affiliated's questionable viability as a going concern. *Id.* Commercial Union claims that this indicated Fidelity's doubtful collection on the accounts, a fact which should have been disclosed in Fidelity's financial statements. *Id.*

[27] *Id.* at 315.

[28] *Id.* at 325.

[29] *Id.* at 323. The trial court granted instruction D-6 which utilized the reasonably foreseeable third party standard. *Id.*

[30] *Id.* at 324. The court relied upon Robinson v. Howard Bros., 372 So. 2d 1074 (Miss. 1979). In *Robinson*, a store employee negligently sold a gun to a minor who later shot Robinson. The court determined that the minor's intentional criminal act broke the causal connection between the negligent sale and the fatal injury. *Id.* at 1076. Similarly, in the instant case, the court concluded that the criminal conduct of Fidelity's president broke the causal connection between Touche Ross' negligence and Commercial Union's pecuniary injuries. *Touche Ross*, 514 So. 2d at 324. *See also* Mississippi City Lines v. Bullock, 194 Miss. 630, 13 So. 2d 34, 36 (1943)(intervening cause relegates original negligence to remote, non-actionable cause).

[31] *Touche Ross*, 514 So. 2d at 322.

[32] The *Ultramares* doctrine originates from the seminal case of Ultramares Corp. v. Touche, 255 N.Y. 170, 174 N.E. 441 (1931), where a lender relied upon negligently prepared financial statements. The court refused to impose liability finding that exposure to an indeterminate number of users of the audit was unwarranted. *Id.* at 179. This doctrine was recently affirmed in Credit Alliance Corp. v. Arthur Anderson & Co., 65 N.Y.2d

2. The foreseen third party standard as expressed in the *Restatement (Second) of Torts* § 552 (1977);[33]
3. The balancing test enunciated in *Biakanja v. Irving*;[34] and
4. The reasonably foreseeable third party standard applied in *H. Rosenblum, Inc. v. Adler*.[35]

In rejecting the *Ultramares* doctrine,[36] the court concluded that the prohibition of a privity requirement by section 11-7-20[37] of the Mississippi Code prevented application of the known third party approach.[38] Likewise, the court discarded the *Restatement* view because its limitation of liability to foreseen third parties was too similar to requiring privity.[39] Foregoing analysis of the balancing test approach,

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536, 483 N.E.2d 110 (1985) with the court concluding that the parties' relationship must sufficiently approach privity before a duty will be imposed. *See also* McLean v. Alexander, 599 F.2d 1190, 1198 (3rd Cir. 1979)(utilized *Ultramares* doctrine under Delaware law); Stephens Industries Inc. v. Haskins & Sells, 438 F.2d 357, 360 (10th Cir. 1971)(applied *Ultramares* doctrine based on Colorado law); Investment Corp. of Fla. v. Buchman, 208 So. 2d 291, 294 (Fla. Dist. Ct. App. 1968)(required privity under Florida law).

[33] The RESTATEMENT view is very similar to that expressed in *Ultramares*. Under this standard the scope of potential plaintiffs is limited to the auditor's client and those whom he knows will be supplied the information by his client. RESTATEMENT (SECOND) OF TORTS § 552 comment (1977). Thus, the auditor must specifically know the relying third party. *Id.*

Numerous jurisdictions have adopted this view, including: Georgia, Badische Corp. v. Caylor, 356 S.E. 2d 198 (Ga. 1978); Iowa, Ryan v. Kanne, 170 N.W. 2d 395 (Iowa 1969); and Ohio, Haddon View Investment Co. v. Coopers & Lybrand, 436 N.E. 2d 212 (Ohio 1982).

[34] 49 Cal.2d 647, 320 P.2d 16 (1958). The California Supreme Court stated that the appropriate analysis involves the balancing of various factors including the foreseeability of harm, the certainty of injury, and the policy of preventing future harm. *Id.* at 19. *See also* Aluma Kraft Mfg. Co. v. Elmer Fox & Co., 493 S.W. 2d 378, 383 (Mo. Ct. App. 1973)(applied *Biakanja* balancing test); Raritan River Steel Co. v. Cherry, Bekaert & Holland, 339 S.E. 2d 62, 69 (N.C. Ct. App. 1986)(*Biakanja* test prevents arbitrary determination of liability).

[35] *See supra* note 15.

[36] *Touche Ross*, 514 So. 2d at 321.

[37] MISS. CODE ANN. § 11-7-20 (Supp. 1986) reads: "In all causes of action for personal injury or property damage or economic loss brought on account of negligence, strict liability or breach of warranty, including actions brought under the provisions of the Uniform Commercial Code, privity shall not be a requirement to maintain said action." *Id.*

[38] *Touche Ross*, 514 So. 2d at 321.

[39] *Id. See generally* Besser, *Privity? - An Obsolete Approach to the Liability of Accountants to Third Parties*, 7 SETON HALL 507 (1976)(analysis of scope of auditor's liability); Note, *Negligent Misrepresentation and the Certified Public Accountant: An Overview of Common Law*, 18 SUFFOLK U. L. REV. 431 (1984)(arbitrary limit on class of potential plaintiff under *Restatement* rule is similar to privity requirements).

the court adopted the reasonably foreseeable third party standard.[40] The court noted that, although the auditor is not the financial statement's guarantor,[41] any resulting losses will be shifted from the innocently relying third party to the negligent auditor.[42] In conclusion, the court's adoption of this standard will protect the third party who relies upon the requested information and insulate the auditor from liability to an unlimited amount of potential users.

II. Discoverability of Trade Secrets

In *American Tobacco Co. v. Horton*[43] the Mississippi Supreme Court extended the scope of discovery to include a manufacturer's trade secrets and other research, development, and commercial information.[44] However, the court affirmed the issuance of a protective order, which tailored the disclosure to specific authorized persons.[45]

Nathan Horton, a longtime smoker of "Pall Mall" cigarettes manufactured by American Tobacco, died of lung cancer allegedly caused by his smoking habit.[46] Ella Mae Howard and Nathan Horton, his widow and son, brought this wrongful death suit against American Tobacco Company and a local distributor in the Circuit Court of Holmes County, Mississippi.[47] During discovery Horton requested responses to interrogatories, including interrogatory No. 8,[48] which sought all relevant information regarding the chemical composition of "Pall Mall" cigarettes and their physical effect on humans.[49] American objected, claiming that the information was proprietary, confidential, and irrelevant to the issues of the case.[50] Thereafter, Horton filed a motion to compel disclosure.[51] Again, American objected, maintaining that the requested information was a highly valued trade secret, the disclosure of which would cause substantial economic injury.[52] On April 7, 1987, the circuit court entered a protective order requiring American to disclose the identity of the ingredients of the "Pall Mall" cigarettes.[53] In response, American applied to the supreme court for a writ of prohibition seeking a reversal of the trial court's disclosure order.[54] The Mississippi Supreme Court affirmed, and denied the writ of prohibition.[55] The court determined that under the facts of this case, the requested information was discoverable[56] subject to the protective order limiting disclosure to authorized persons.[57]

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[40] *Touche Ross*, 514 So. 2d at 322.

[41] *Id.*

[42] *Id.*

[43] 508 So. 2d 1057 (Miss. 1987).

[44] *Id.*

[45] *Id.*

[46] *Id.*

[47] *Id.* at 1060. Horton's complaint alleged a strict liability tort claim that American manufactured and distributed cigarettes which were unreasonably dangerous or defective the consumption of which caused his death. *Id.*

[48] *Id.* at 1058. The interrogatory sought identification of the scientific and generic names and the chemical formula of all chemicals and additives in the "Pall Mall" cigarette. *Id.* It further requested information as to whether any ingredients had been determined or suspected of being cocarcinogenic, carcinogenic, a tumor initiator, or to yield nitrosamines. *Id.* Finally, it sought any information on tests and research done to determine the properties and health hazards of the product. *Id.*

[49] *Id. See supra*, note 48.

[50] 508 So. 2d at 1058.

The court first addressed the appropriateness of the procedural vehicle - the writ of prohibition - in seeking the requested relief.[58] In concluding that its use was proper,[59] the court stated that the writ initiates an extraordinary proceeding and vests a superior court with jurisdiction so as to prevent some "palpable and irremedial injustice."[60] Under this standard, the court concluded that it had jurisdiction to settle the question.[61]

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[51] *Id.*

[52] *Id.* American supported its motion with an affidavit which contained the following assertions: (1) "Pall Mall" is one of the most popular cigarettes; (2) "Pall Mall" contains flue-cured, air-cured, and oriental tobaccos, humectants, proprietary flavorings and paper wrapping; (3) the formula of the additives is kept in a vault with access limited to 20 employees who are further limited as to the number of times access is allowed; and (4) the additives formula has never been revealed to the public. *Id.* Based on these facts, American argued that compelled disclosure of its highly valuable proprietary information would cause substantial economic harm. *Id.*

[53] *Id.* The protective order limited access to the information to the plaintiff and any experts being retained or consulted in preparation of the case. *Id.* Further, the order allowed disclosure to these experts only if plaintiff's counsel, in good faith, deemed it necessary. *Id.*

[54] *Id.* at 1059.

[55] *Id.* at 1057

[56] *Id.*

[57] *Id.*

[58] *Id.* at 1059. Authority for a writ of prohibition is found in MISS. CODE ANN. § 11-41-1 (1972). *See also* Pearl River Valley Water Supply Dist. v. Brown, 248 Miss. 4, 24-25, 158 So. 2d 694, 695 (1963)(writ is remedy geared to prohibit inferior court or judge from exercising jurisdiction improperly).

[59] *Horton*, 508 So. 2d at 1059.

[60] *Id. See* State v. Maples, 402 So. 2d 350, 352 (Miss. 1981)(writ may be issued to prevent irreparable action of inferior judge). *See also* State ex rel. Pittman v. Griffin, 450 So. 2d 426, 428 (Miss. 1984)(writ of prohibition is remedial writ); Fondren v. State Tax Comm'n, 350 So. 2d 1329, 1332 (Miss. 1977)(although writ usually available only to attorney general or district attorney, may be available to private citizen upon showing of irremediable interest in excess of general public's interest).

Addressing the principle issue, the court initially set forth the two competing interests in the case: (1) American's right to prevent indiscriminate disclosure of confidential proprietary information;[62] and (2) Horton's right of access to information granted by Rules 26 and 33 of the Mississippi Rules of Civil Procedure.[63] Noting the plaintiff's allegation as one of strict liability requiring proof of an unreasonably dangerous or defective product,[64] the court refused to allow American to restrictively amend Horton's claim in a manner which would render irrelevant the discovery of the requested information.[65] Moreover, the court observed that the requested information was necessary to obtain the expert evaluation of whether the ingredients are defective or unreasonably dangerous.[66] However, the court emphasized that an objective judicial determination of necessity before a party may obtain information in discovery has never been required.[67] Furthermore, the court stated that there was no trade secret exception to the general scope of discovery as defined by procedural Rule 26(b)(1).[68] In sum, the court concluded that the information sought was discoverable.[69]

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[61] *Horton*, 508 So. 2d at 1059.

[62] *Id.* The court explained that this information is a recognized property right under our system of laws. *Id. See* Electric Reduction Co. of Canada, Ltd. v. Crane, 239 Miss. 18, 31, 120 So. 2d 765, 770 (qualified privilege to refuse to disclose trade secrets in deposition). *See also* Cataphote Corp. v. Hudson, 444 F.2d 1313, (5th Cir. 1971)(trade secrets need not be so unique or novel as to be patentable; need only possess sufficient originality to separate them from everyday knowledge). Also, the court noted that trade secrets are a form of intangible property in which the law provides protection from interference or unlawful access by others. *Horton*, 508 So. 2d at 1059-60. *See* Electric Reduction Co. of Canada, Ltd. v. Crane, 239 Miss. 18, 120 So. 2d 765 (1960). *See also* Cataphote Corp. v. Hudson, 444 F.2d 1313 (5th Cir. 1971).

[63] *Horton*, 508 So. 2d at 1060. *See* Miss. R. Civ. P. 26 (defines general scope of discovery); Miss. R. Civ. P. 33 (interrogatories).

[64] *Horton*, 508 So. 2d at 1060.

[65] *Id.* American attempted to redefine Horton's claim as alleging that the smoke caused his death thus rendering irrelevant the identification of the additives in the cigarettes. *Id.* The court emphatically refused. *Id.*

[66] *Id.* at 1060-61.

[67] *Id.* at 1061.

[68] *Id. See* Federal Open Mkt. Comm. v. Merrill, 443 U.S. 340, 362-63 (1979) (although Federal Reserve's Domestic Policy Directives contain confidential information, they are not protected from civil discovery process); Centurion Indus., Inc. v. Warren Stevrer & Assoc., 665 F.2d 323, 325-26 (10th Cir. 1981) (trade secrets relevant to patent infringement case discovery); Coca-Cola Bottling Co. v. Shreveport Inc., 107 F.R.D. 288, 294-95 (D. Del. 1985)(Coca-Cola formula discoverable to ascertain whether product was covered by pricing agreement).

[69] *Horton*, 508 So. 2d at 1061.

Although the court permitted the requested discovery,[70] it determined that the trial court was correct in granting American's request for a protective order.[71] Relying upon Mississippi procedural Rule 26(d)(7),[72] the court explained that the circuit court is responsible for proper compliance with the order.[73] In conclusion, the court denied the writ of prohibition and permitted the requested discovery under the limitations of the protective order.[74] By so ruling, the court served both party's interests: Horton's rights of access to information and American's claim for protection of a property interest.

III. EVIDENCE IN MEDICAL MALPRACTICE ACTIONS

In *Thompson v. Carter*,[75] the Mississippi Supreme Court addressed two important evidentiary questions: (1) the admissability of a non-physician's expert testimony to establish the standard of care regarding the use of pharmaceutical drugs;[76] and (2) the conditions under which a package insert accompanying a prescription drug may be admitted into evidence.[77]

On February 7, 1976, Thompson went to Howard Memorial Hospital in Biloxi, Mississippi after suffering from a persistent pain for two days.[78] She was admitted to the hospital after the initial examination revealed blood and pus in her urine.[79] In her admissions report, Thompson reported no history of known allergies to drugs.[80]

Dr. Robert Carter, a urologist, diagnosed Thompson as having a kidney infection which appeared to be both acute and chronic.[81] Carter prescribed Bactrim, a type of antibiotic, to treat the infection.[82] Thompson continued to take the medication and began to experience flu-like symptoms including a sore throat, mouth sores, and persistent coughing.[83] She ceased taking Bactrim in early March after Dr. Carter concluded that she was well from her kidney infection.[84] However, soon thereafter, her health deteriorated, and on March 8, 1976, she was hospitalized and diagnosed as having Stevens Johnson Syndrome, a severe allergic reaction.[85]

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[70] *Id.*

[71] *Id.*

[72] *Id. See* MISS. R. CIV. P. 26 (d)(7)(protective order).

[73] *Horton*, 508 So. 2d at 1061.

[74] *Id.* at 1062. *See supra* note 53.

[75] 518 So. 2d 609 (Miss. 1987).

[76] *Id.* at 613-615.

[77] *Id.* at 612-13.

[78] *Id.* at 610.

[79] *Id.*

[80] *Id.*

[81] *Id.* Carter specifically diagnosed this infection as being pyelonephritis secondary to pyelitis cystics. *Id.*

[82] *Id.* Bactrim is a sulfonamide antibiotic produced by Roche Laboratories. *Id.* Carter instructed her to take two tablets per day. *Id.*

In June of 1979, Thompson filed suit against Carter claiming that his negligent prescription of Bactrim caused her ensuing injuries.[86] The trial court directed a verdict in favor of Carter because Thompson failed to provide expert medical testimony.[87] On appeal, the Mississippi Supreme Court reversed and remanded for a new trial.[88] The court concluded that the trial court erroneously failed to admit the package insert and the testimony of the plaintiff's medical expert.[89]

First, the court addressed the admissability of the package inserts. Under Rule 803 (17) of the Mississippi Rules of Evidence,[90] the court concluded that the package inserts were published compilations generally relied upon by the public which are excepted from the rule against hearsay.[91] The court found that these package inserts were the basis of a Food and Drug Administration regulatory system for notification of information on the use of prescription drugs.[92] After finding that Dr. Carter did rely upon the inserts when prescribing the medication,[93] the court held that the inserts should have been admitted into evidence.[94]

After finding the inserts admissible, the court then analyzed for what purpose the inserts may be used.[95] Although one jurisdiction allowed use of the inserts as proof of the professional standard of care,[96] the court refused to adopt such a rule.[97] Recognizing that these inserts are also a marketing and merchandising tool,[98] the court determined that the inserts should not be taken as conclusive evidence of the physician's standard of care, nor should failure to adhere to the insert's instructions be considered to establish a prima facia case of negligence.[99] In conclusion, the court held that the package inserts contain prima facia proof of the proper method of use of bactrim and were admissible at trial for those purposes only.[100]

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[83] *Id.*

[84] *Id.*

[85] *Id.* at 611. Thompson began experiencing severe swelling, red bumps over her entire body, and blisters formed in her mouth and genitals. *Id.*

[86] *Id.* Thompson also sued Roche Laboratories under breach of warranty, negligence, and strict liability theories. However, soon thereafter, she elected a voluntary nonsuit against Roche but continued her action against Carter. *Id.*

[87] *Id.*

[88] *Id.* at 615.

[89] *Id.*

[90] Miss. R. Evid. 803 (17).

[91] *Thompson*, 518 So. 2d at 615. *See also* Yazoo & M.V.R. Co. v. M. Levy & Sons, 141 Miss. 199, 106 So. 525, 527 (1925)(cotton exchange reports were admissible).

[92] *Thompson*, 518 So. 2d at 611-612.

[93] *Id.* at 612.

[94] *Id.*

[95] *Id.* at 612-613.

[96] *See* Otiligschlager v. Proctor Community Hospital, 303 N.E. 2d 392, 396 (Ill. 1973)(explicit instructions furnished by manufacturer for proper manner of intravenous injection and warnings of hazards accompanying its improper administration provide

Finally, the court addressed the question of whether a person who does not have a medical degree is qualified to testify concerning the standard of care to which physicians are to conform when administering drugs. In the instant case, the trial court excluded the testimony of Michael P. Hughes, a person possessing master's degrees in both Pharmacology and Toxicology.[101] Reasoning that an expert need only possess medical knowledge which will assist the trier of fact in understanding the evidence or determining a fact in issue,[102] the Mississippi Supreme Court held that Mr. Hughes was qualified to testify on the issue of a physician's standard of care notwithstanding his lack of a medical degree.[103] However, the court limited this to witnesses who possess scientific, technical, or specialized knowledge on the particular topic about which he is to testify.[104] Therefore, the court concluded that Mr. Murphy's testimony was erroneously excluded and remanded

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proof of proper professional standard ordinarily shown by expert medical testimony).

[97] *Thompson*, 518 So. 2d at 612-613.

[98] *Id.*

[99] *Id.*

[100] *Id. See* Julien v. Barker, 272 P.2d 718, 724 (Idaho 1958)(package insert is prima facia evidence of method of use provided by manufacturer).

[101] *Thompson*, 518 So. 2d at 613-14. Hughes had much experience in his field. He had been coordinator for the Regional Control Center during which time he was frequently consulted by physicians regarding treatment of poison victims and other adverse reactions to drugs. He also taught at both the University of Mississippi medical and dental schools in pharmacology and toxicology. *Id.* at 615.

[102] *Id.* at 614; *see* Anchor Coatings, Inc. v. Marine Indus. Res. Insul. Inc., 490 So. 2d 1210, 1217-18 (Miss. 1986)(qualification of an expert); Hardy v. Brantley, 471 So. 2d 358, 366 (Miss. 1985)(expert must possess special knowledge that aids finder of fact); Hall v. Hilbun, 466 So. 2d 856, 873-874 (Miss. 1985)(expert opinion testimony proper if expert possesses knowledge which will aid trier-of fact).

[103] *Thompson*, 518 So. 2d at 615. Other jurisdictions have adopted this same rule of law. *See* Cornfeldt v. Tongon, 262 N.W. 2d 684, 697 (Minn. 1977)(nurse allowed to testify as expert regarding the use of anesthesia); Hudgins v. Serrano, 453 A.2d 218, 223-24 (N.J. 1982)(medical license not required for person to testify as medical expert in malpractice case).

[104] *Thompson*, 518 So. 2d at 615.

the case for a new trial.[105]

In a lengthy dissent, Justice Dan Lee objected to the majority opinion on three points: (1) the majority allowed the negligence issue to reach the jury without the plaintiff establishing a prima facia case; (2) it allowed use of the package inserts as "some" evidence of standard of care absent expert medical testimony; and (3) that a non-medical doctor is now qualified to testify that because a patient suffers an unforeseen allergic reaction, the doctor should not have prescribed the medicine.[106] The dissent noted that two essential elements were conspicuously missing - evidence of the standard of care and evidence of the breach of that standard of care.[107] The dissent argued that the majority wrongfully glossed over these requirements by couching the issue in terms of causation.[108] The dissent concluded that this analysis wholly failed to follow precedent by allowing a non-medical expert and information contained in the package inserts to be evidence of a physician's standard of care.[109]

Wink Glover

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[105] *Id.*

[106] *Id.* at 616.

[107] *Id.* at 620.

[108] *Id.* at 617.

[109] *Id.* at 620-21.

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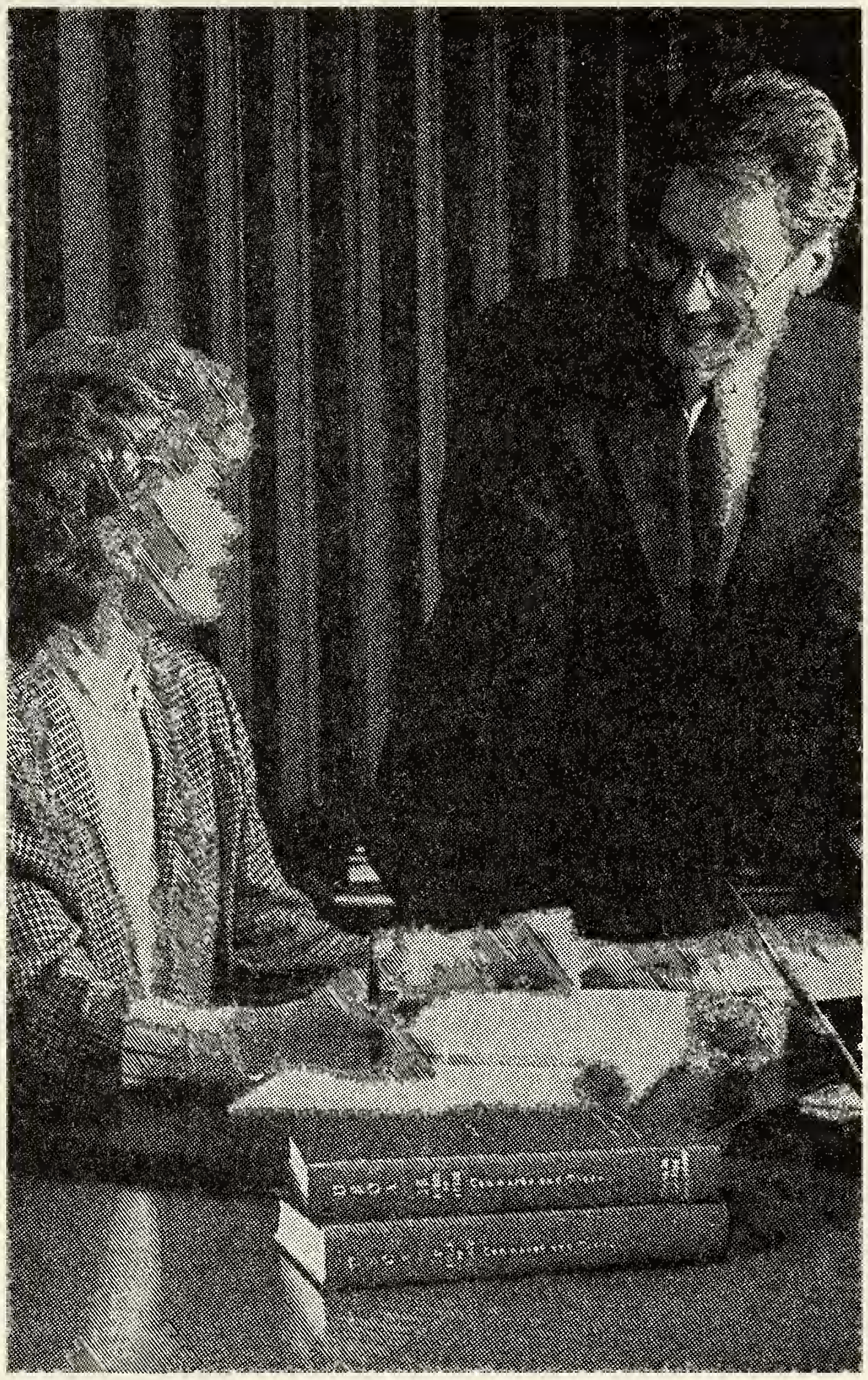

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